



Building a better AA

AA plc Annual Report
and Accounts 2018

AA

FINANCIAL HIGHLIGHTS

Trading revenue

£959m

2017: £940m

Trading EBITDA

£391m

2017: £403m

Profit before tax from continuing operations

£141m

2017: £100m

Free cash flow to equity

(£5m)

2017: £97m

Net debt

£2.7bn

2017: £2.7bn

Continuing adjusted basic EPS

21.8p

2017: 21.3p

Continuing basic EPS

18.2p

2017: 12.2p

Interest cover

2.8x

2017: 2.6x

Total announced dividend per share

5p

2017: 9p

READ MORE IN THE
FINANCIAL REVIEW
P27

A message from Simon Breakwell, our new Chief Executive Officer



As I write to our shareholders, I am very conscious of what a difficult year it has been for you and I deeply regret what many of you have had to go through. However, at the same time, I am convinced that the AA is in a stronger position now. We have acknowledged our weaknesses and have been realistic about our strengths and, as a result, have been able to define a more sustainable future.

There is much to commend in the way in which the AA responded following the departure of our former Executive Chairman. The AA's people responded by simply getting on with their jobs. I have received huge support in undertaking a rigorous review of the business and in developing the new strategy. As we have commenced making the very substantial changes needed, the commitment of our people to renewing this great organisation has been inspiring.

It was not an immediate decision for me to take on this role. I began as Acting CEO, fully expecting to hand over to a new permanent CEO in time. However, as I deepened my understanding of the wonderful company that is the AA, I decided to take on the permanent role when it was offered to me. I was very struck by the ethos of our people, front line and back office, and their commitment to our cause. I was also inspired from the perspective of my tech background by the potential for modernising the AA.

Our new strategy will put service, innovation and data at the heart of the AA. We want, once again, to ensure our members, policy holders and customers get something beyond breakdown cover and that they benefit from their membership. Our values capture the way in which we will deliver this: care and courtesy, expertise, collaboration and dynamism really do sum up our approach to all we do.

I look forward with excitement to creating a better AA. This is the time to make the AA relevant and sustainable in what it represents for its members and customers. This annual report sets out our thinking on what we can achieve and how we plan to do it.

Simon Breakwell
Chief Executive Officer

READ MORE:
CHIEF EXECUTIVE'S
STRATEGIC REVIEW
P12

READ SIMON'S ANSWERS
TO SHAREHOLDERS
QUESTIONS **P18**

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We have strong fundamentals upon which to build a better AA and deliver sustainable returns

A highly trusted commercial brand

The AA has one of the most widely recognised and trusted brands in the UK, building on more than 110 years of service and innovation.

Market leadership

The AA is by far the largest roadside assistance provider with approximately 40% share of the UK consumer market and c.65% share of the business-to-business (B2B) market. While our share in Insurance is small, our brand is the most highly considered for motor insurance.

Opportunity for digital transformation

We are at the forefront of digital development in our sector with the potential to transform the services we deliver and the experience our members and customers receive.

High barriers to entry

Our deployment system, people and scale combined with the high start-up costs required to operate an efficient national roadside service pose significant barriers to entry.

High recurring revenue

Our personal members are loyal with a stable retention rate of 82% and average tenure of 12 years.

Strong cash generation

The majority of our customers pay for our services in advance so that virtually all of our profits convert to operating cash flow.

Excellent standards of service delivery

We have more patrols than our competitors, with excellent training, equipment and technology providing the UK's premium roadside assistance service.

Unlocking the full potential of the AA

We will deliver targeted and strategic investment in our people, our products, our systems and operations, building on the solid foundation that our investments have created since the IPO. The focus of the new strategy is to:

1

Innovate and grow Roadside, developing our connected car positioning

2

Accelerate the growth of Insurance

3

Improve the efficiency, predictability and resilience of Roadside

4

Create a culture capable of delivering excellent performance and executing the strategy



PUTTING SERVICE, INNOVATION
AND DATA AT THE HEART OF THE
AA P14

With the additional investment, Trading EBITDA expectations are 12% to 14% lower for FY19; however, despite this, we expect to remain cash generative in FY19.

This investment provides a strong base for future growth in both profits and cash generation. Our financial strategy remains to reduce the cost of borrowing and to de-lever with an overall target of lowering our leverage to between three and four times over the medium to long term.

As a result of the investment, and the operation of the dividend gating covenant associated with our borrowings, the Board has changed its policy on dividends, proposing to pay 2p per share per year from FY19 until such time as it is satisfied that the profit and free cash flow enable a change in policy.



READ MORE ON
FINANCIAL
REVIEW P27

Chairman's statement

Committed to good governance principles



We acknowledge and regret that shareholders have had a very difficult year and that you – and the Company itself – deserve better. We believe we are now in a position to build a better AA.

I am delighted that Simon Breakwell has taken over as CEO. He is already leading this great Company into a new era, building on what is good and changing what is not. He also has the background and experience to develop our digital positioning and, in particular, to lead the redesign and re-engineering needed for our emergent connected car products and services.

This has been a challenging year for the Board in which we had no choice but to take decisive action to remove our former Executive Chairman, Bob Mackenzie, for gross misconduct. We see it as a positive development that we now have a normal board structure and are delighted that Cathryn Riley has joined it, adding expertise and strength.

We believe the new strategy is the right one. It is an evolution of the previous strategy, but with a simplified focus, strong leadership and a supportive culture, we believe that, at last, we have what we need to deliver our strategy.

John Leach
Chairman



Our performance and the strategic review

While these results are in line with our guidance, they demonstrate the challenges we face.

Trading EBITDA is down compared with last year because we could not achieve the growth in revenue without additional cost. In a nutshell, this is the challenge our new strategy addresses.

However, the AA has the fundamental strengths which its brand and market leadership give it. In combination with the investments made since the IPO, these give us strong foundations on which to build our new strategy.

Roadside has demonstrated these fundamental strengths. We grew new business once again and maintained member retention despite the pressures we faced. The use of the app has gone from strength to strength, and Car Genie, our first step into connected car technology, was launched in August 2017. Insurance has demonstrated its ability to grow with the support of our in-house underwriter.

When Simon took over as CEO on 25 September 2017, he began a rigorous review of the business which resulted in the strategy presented to the markets on 21 February 2018.

We considered two options:

We could have continued on the track we were on in Roadside. To achieve growth we would increasingly have relied on price increases as well as reductions in investment in marketing, IT and the membership proposition. Without investment in Insurance, we could not grow that business either. While membership, insurance policies and profitability would have been relatively stable initially, over time they would have declined.

The other option, the one the Board selected, was to invest in the three key drivers of future growth – service, innovation and data. Our plan will deliver growth in Roadside and accelerate growth in Insurance. To enable this, we will create a more resilient organisation with a high-performance culture that can deliver excellent and efficient service. This is fully explained in the strategy section on pages 12 to 17.

The Board

On 1 August 2017, Bob Mackenzie was removed from his role as Executive Chairman, his other roles as a director, and employee of the Group, for gross misconduct.

Simon Breakwell's appointment, initially as interim CEO, expedited the split in the roles of CEO and Chairman which was already our stated intention. I became Chairman, relinquishing the role of Senior Independent Director (SID) which I had held since 13 November 2014 and which Andrew Blowers took over.

Simon, who joined the AA in September 2014 as a Non-Executive Director, stepped down from his previous Committee roles once he became an Executive Director.

Cathryn Riley was appointed a Non-Executive Director on 28 February 2018. Cathryn was previously Chair of our insurance broker, AA Insurance Services Limited (AAISL) and we will continue to benefit from her wide-ranging experience which covers insurance, customer services, IT, operations and human resources.

The appointment of Cathryn Riley has increased the size of the Board, but until additional non-executive directors are appointed, my involvement is required on several committees, including Audit which I will leave as soon as they are appropriately resourced and there has been a smooth handover.

The Board roles are now as follows:

- › I remain Chair of the Nomination Committee and a member of the Risk, Remuneration and Audit Committees
- › Simon Breakwell is our Chief Executive Officer
- › Martin Clarke continues as Chief Financial Officer
- › Andrew Blowers is the new SID and is Chair of the Risk Committee and a member of the Audit and Nomination Committees
- › Suzi Williams is Chair of the Remuneration Committee and is also on the Nomination and Risk Committees
- › Andrew Miller will retire from the Board at the AGM on 7 June 2018 but continues until then as Chair of the Audit Committee and member of the Risk and Remuneration Committees. We thank him for his contribution and support
- › Cathryn Riley is a member of the Risk Committee

Our Company Secretary, Mark Millar, has chosen to return to private legal practice and steps down on 17 April 2018. Martin Clarke will hold the role however, Mark Millar will continue to support us, until our new Company Secretary, Nadia Hoosen, joins us from TalkTalk in the summer.

It is important that the Board's achievements during the year are not overshadowed by the removal of Bob Mackenzie. A strong governance framework is requisite for the delivery of the new strategy and I shall continue to provide advice and oversight on governance.

We conducted our first external Board evaluation during the second half of 2017. It was undertaken by Condign Board Consulting, which concluded that the Board and the Committees were operating effectively and that the separation of the CEO's and Chairman's roles had produced immediate improvements. For further details of the evaluation process and action plan see page 58.

Remuneration

When Simon became CEO, he vacated the Chair of the Remuneration Committee which has been taken on by Suzi Williams. As we have recovered the MVP shares held by the former Executive Chairman, we move from the legacy scheme to use our more typical Performance Share Plan and more usual PLC remuneration structures.

Dividend

As announced in February, the Board has changed its policy on dividends as a result of the investment associated with the new strategy and the operation of the dividend gating covenant under the Whole Business Securitisation (WBS) debt structure.

We propose a dividend of 2p per share per year from FY19, until such time as the Board is satisfied that the profit and free cash flow enable a further change in policy.

In view of this, the Board is recommending a final dividend in respect of FY18 of 1.4p per share, subject to approval at the AGM on 8 June. Added to the interim dividend already paid, recommended total dividends for FY18 are 5p per share.

We currently expect the dividend in respect of FY19 to be split 0.6p per share for the interim and 1.4p per share for the final.

Our culture – and our thanks

The AA is a wonderful company and I urge you to read the comments from our Employee Award winners on pages 20 to 21 to get a sense of the energy and enthusiasm with which our people do their jobs. This is despite very poor employee engagement levels, which we have ascertained from the first employee survey for many years.

We have made employee engagement a key performance measure for our leaders and we expect to see an improvement.

I thank all the AA teams for their work this year, a year which has been as difficult for us as it has been for our shareholders, and in which we made extra demands on everyone to work harder. They did and we deeply appreciate it.

Meeting shareholders

We fully recognise that the relationships with our shareholders are critical to successful governance and as Chairman I continue the role I had as SID as key point of contact for shareholders. We are grateful to those who have engaged with us and we will continue to conduct meetings to enable major shareholders to meet members of our Board and the Company Secretary. I also encourage shareholders to attend the Annual General Meeting. In addition, Andrew Blowers, our new SID, and I offer an open invitation to our shareholders to contact us. Please do so through the Company Secretary or Investor Relations.



John Leach
Chairman

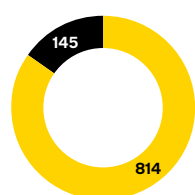
At-a-glance

What we do

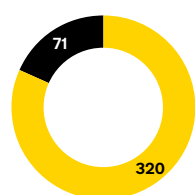
In line with our new strategy, we have altered our segmental reporting. Roadside Assistance and Driving Services are now shown together as Roadside. Insurance Services, which includes Financial Services, and Insurance Underwriting are now combined as Insurance. We are allocating head office costs to these two divisions. A reconciliation between old and new reporting is provided on page 26.

New divisions

TRADING REVENUE (£m)



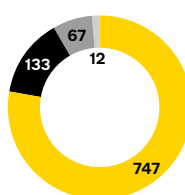
TRADING EBITDA (£m)



● Roadside ● Insurance

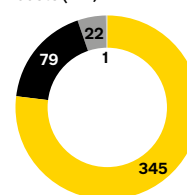
Previous divisions

TRADING REVENUE (£m)



● Roadside Assistance ● Insurance Services ● Driving Services ● Insurance Underwriting

TRADING EBITDA before Head Office costs (£m)



ROADSIDE



We are the UK's leading provider of roadside assistance, with approximately 2,900 patrols attending an average of around 10,000 breakdowns daily. Driving Services comprises our market-leading driving schools AA Driving School and BSM, and DriveTech, the market leader in driver education including Driver Awareness courses which are offered by police forces.

Trading revenue

£814m

2017: £809m

Personal members

3.3m

2017: 3.3m

Driving instructors

2,742

2017: 2,607

Trading EBITDA

£320m

2017: £337m

Business customers

9.9m

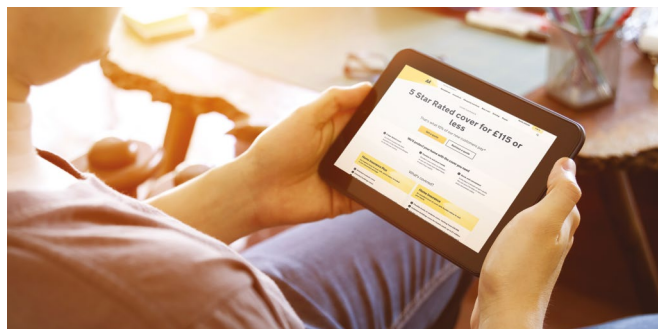
2017: 10.0m

DriveTech police contracts

11

2017: 11

INSURANCE



The AA's insurance broker focuses primarily on motor and home policies, operating a diverse panel of underwriters including our in-house underwriter. It includes our Financial Services partnership with the Bank of Ireland and our Home Emergency Services business which we have sold. We launched our in-house underwriter in January 2016 and underwrite both motor and home policies, reinsuring 80% of the risk.

Trading revenue

£145m

2017: £131m

Insurance policies

1.4m

2017: 1.5m

Financial Services products

142,000

2017: 100,000

Trading EBITDA

£71m

2017: £66m

Underwritten policies

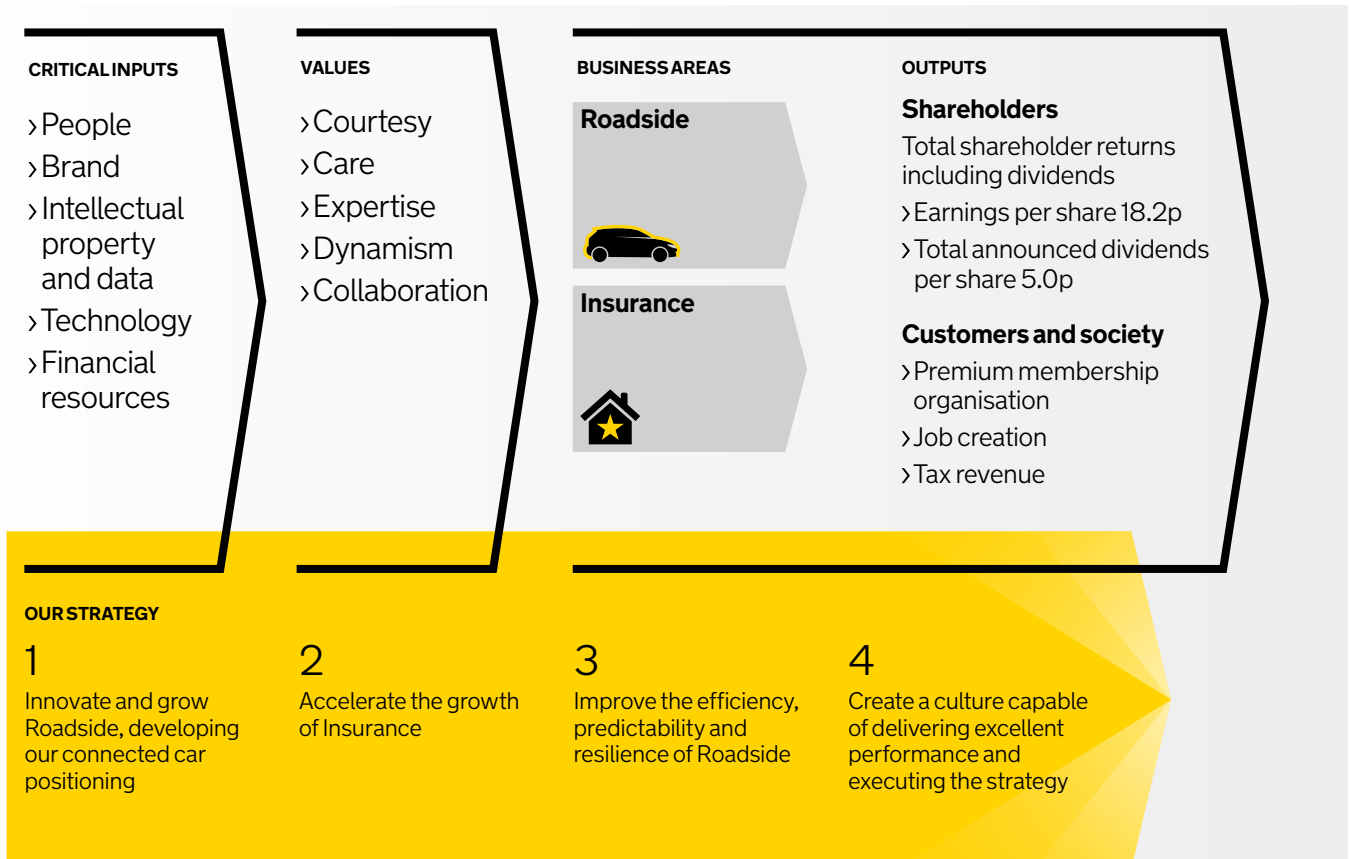
407,000

2017: 140,000

Our business model

The UK's pre-eminent membership services organisation

Our business relies on critical inputs which we manage and deploy based on the strategy of the business. These are underpinned by our core values.



Our business model

continued

Roadside



WHAT WE DO AND HOW WE COMPETE

Personal membership

We provide breakdown cover for our consumer members. Vehicle-based policies cover only a specific vehicle and personal memberships cover one or more individuals, including families, regardless of the vehicle.

Competitive landscape

The roadside recovery market continues to grow as the car parc expands but it is relatively mature and competitive. The sector is dominated by three major players, of which the AA is the largest. Our competitive advantage is based on quality of service, brand consideration, distribution platform as well as digital capability. New trends are emerging which the AA is well placed to take advantage of, given its leading market position, its technology and our early steps in connected car development.

The AA is the market leader with approximately 40% of the consumer market, followed by RAC and Green Flag.

Business to business

For our 10 million business (B2B) customers, breakdown cover is provided by manufacturers for new cars for an average of two years, by banks for premium added value account holders (AVAs), or by managers of fleets and vehicle leasing companies. However, the service is delivered by the AA. The majority of these are pay-for-use contracts.

Competitive landscape

The business-to-business roadside assistance market earns lower margins but, as these contracts are sophisticated in their specification, barriers to entry are high and our leading position is based on our high service levels and ability to innovate.

The AA has approximately 65% of the manufacturer segment, over 60% of the UK's largest fleet and leasing companies and around half of the banking AVA segment.

Driving services

We have integrated our driving schools and DriveTech business into Roadside. The driving schools business offers franchises to qualified driving instructors under the AA Driving School and British School of Motoring (BSM) brands. The DriveTech business offers training for occupational drivers and drivers who have committed driving offences.

Competitive landscape

The UK driving schools market is highly competitive and fragmented, but we have approximately 10% of this market. Our main competitors are Red and Bill Plant.

In relation to the DriveTech business, the AA has strong positions in both fleet and police markets. Our main competitor in this market is TTC. In the fleet market the AA is market leader and has a range of smaller competitors who compete primarily on price.

THE VALUE THIS CREATES

Revenue model

Consumer Roadside Assistance fees are principally paid through annual or monthly subscriptions. Additional revenue is available from cross-selling (selling other services) or up-selling (selling higher value products and services).

Performance indicators

Paid personal members
3.3m (FY17: 3.3m)

Average income per member
£157 (FY17: £158)

Number of breakdowns attended 3.7m (FY17: 3.6m)

Revenue model

B2B fees are either set per breakdown or per vehicle. The average tenure of the contracts varies ranging from three to five years.

We are working on a number of developments with our manufacturer partners and expect to generate additional revenue from providing new services and our technical know-how to enable them to improve their offering.

Performance indicators

Business customers
9.93m (FY17: 9.98m)

Average income per customer
£20 (FY17: £20)

Revenue model

The AA and BSM driving schools' revenue derives from franchise fees from instructors for use of branded cars and the AA's booking system. The cars are funded by the AA under a finance lease arrangement. We also provide training for driving instructors.

In relation to the DriveTech business, our driver training services are delivered under long-term service contracts.

Performance indicators

Franchised driving instructors
2,742 (FY17: 2,607)

MANAGING OUR RISKS

Roadside Assistance is a discretionary product for consumers, however our sales process is regulated as it is bought by consumers as insurance. We actively manage risk through our Risk Management Framework which covers the following areas:

- > Member satisfaction levels and good member outcomes
- > Changes to regulatory and fiscal environment
- > Competition from lower priced competitors
- > Information security, cyber crime and data management

Roadside Assistance is provided with warranties for new vehicles, leased vehicles and fleets. It is provided as part of benefits packages for banks' Added Value Account holders. We actively manage risk through our Risk Management Framework which covers the following areas:

- > Partner satisfaction levels
- > Competition
- > Information security, cyber crime and data management

We actively manage our risks through our Risk Management Framework. Within driving schools, this covers the following areas:

- > Customer satisfaction levels
- > Competition from lower priced competitors
- > Information security, cyber crime and data management

Insurance



Broking

The AA's insurance broking business serves both personal members and non-members selling primarily motor and home insurance. These policies are underwritten by panels of underwriters, including the AA's in-house underwriter.

Competitive landscape

Insurance brokers compete largely on the price of premiums. This is particularly true of the 70% of motor insurance sales made through price comparison websites (PCWs). While our brand consideration is highest in motor insurance, price dominates and we have turned around our motor policy book as a result of our improved price competitiveness.

In home insurance PCWs are less dominant in part because home specifications vary more and home insurance is less expensive than motor which reduces churn.

We are a small player in the motor and home market but have plans to grow. Our competitors include Admiral, Hastings and Direct Line Group.

Revenue model

As an insurance broker, the AA acts as an intermediary between those seeking insurance cover and the insurance underwriters. The AA earns commission at the point of sale, from ancillaries and from renewals.

Performance indicators

Total motor and home policies
1.4m (FY17: 1.5m)

Average income per motor and home policy
£74 (FY17: £70)

Broking is regulated. We manage our risk through our Risk Management Framework which covers:

- › Customer satisfaction levels and good customer outcomes
- › Changes to regulatory and tax environment
- › Competition from PCWs
- › Information security, cyber crime and data management

Underwriting

The AA's in-house underwriter launched motor policies in January 2016 followed by home policies in August 2016. As part of the AA Group, we utilise our extensive proprietary data as appropriate to hone our pricing. This enables us to price more competitively which supports the broker's ability to win more business. We are now underwriting 36.5% of our motor broker policies.

Our underwriter has grown rapidly and is in profit with a combined operating ratio (COR) below (and therefore ahead of) our target of 95%.

Competitive landscape

Underwriters compete primarily on price. The combined operating ratios in this underwriting market are just under 100% (thus earning single digit margins) and the integrated model means that our underwriter drives our higher broker volumes.

Revenue model

The underwriter retains 20% of gross written premiums before coinsurance and reinsurance. The in-house underwriter is required to maintain certain levels of solvency capital and as at 31 January 2018, ours was approximately £15m.

Performance indicators

Policies underwritten
407,000 (FY17: 140,000)

Underwriting is regulated. We manage our risk through our Risk Management Framework which covers:

- › Changes to regulatory and tax environment
- › Information security, cyber crime and data management
- › Solvency capital

Financial Services

We launched our partnership with the Bank of Ireland in 2015 to provide savings, loans, credit cards and mortgages on a matched-book basis. We have seen strong growth in our personal loan book, driven by the relevancy of the AA for consumers using loans to purchase cars. Our credit card products have been more challenged, due to the loss of interchange fees and a very competitive market driving very long 0% interest promotional periods.

Competitive landscape

The combination of the AA's brand and distribution platform and the Bank of Ireland's expertise in service delivery gives our partnership a competitive advantage. We expect to grow our book over the life of this ten-year agreement with the Bank of Ireland.

Our main competitors are Virgin Money, Tesco and the High Street Banks.

Revenue model

Investment into the partnership to drive growth is ongoing. When the partnership starts generating profits, these will be shared 50/50.

Performance indicators

Financial Services products
142,000 (FY17: 100,000)

The financial services business is subject to regulation. The Bank of Ireland undertakes the principal regulated activities.



Market context

The opportunities presented by the emerging trends in roadside assistance

Since its inception in 1905, the AA has innovated and been at the forefront of providing the UK consumer with a reliable, trusted, premium roadside assistance service. Today we lead both the consumer and business roadside assistance markets.

The AA has addressed and embraced the many mechanical, economic and technological innovations in the automotive sector over the years, evolving without compromising its commitment to service excellence and core values. Our culture has had to be dynamic to enable patrols to use their personal expertise, supported by innovative developments and equipment, to deliver courteous service with care for the member or business customer and their vehicle. It is this approach which has helped the AA to remain resilient through the economic cycles and which provides the platform for our new strategy.

In addition to technological change over the past quarter of a century, we have seen the growth of lower-margin operators, aggressively offering lower service levels and relying on third-party service providers. Third-party service is not AA branded and is less capable of delivering the high roadside repair rates and levels of customer satisfaction that our patrols do. Our focus on service levels has underpinned our market leadership in both consumer and business markets.

We believe that by remaining true to our values and embracing technological change, we can continue to operate at the premium end of the market and reshape the AA as a digitally-led roadside assistance service provider with a strong and growing insurance business.

We have identified below a number of trends emerging in the roadside assistance market that we are often asked about by investors.

We are confident that these trends represent opportunities for the AA. By leveraging our brand, scale, partnerships and our digital positioning, we can play a leading role in the developments in the automotive sector.

Emerging trend

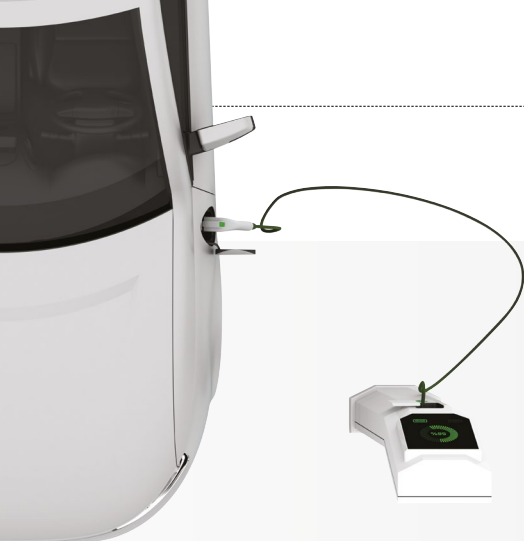
Improving reliability

As cars become more reliable, will customers be less likely to buy roadside assistance cover, thereby gradually rendering the AA roadside assistance business obsolete?

Where we see the opportunity

- › We welcome the increasing reliability of cars. However, the number of breakdowns has been relatively stable over the last decade with a slight increase in the last two years. The decline in mechanical breakdowns has been more than offset by the increase in the number related to maintenance and road conditions. Tyre damage and batteries represent about 1/3rd of total breakdowns.
- › We have been innovative in dealing with the shift in breakdowns, ensuring we have the capability to provide excellent service whatever the problem. Our battery-testing kit and universal spare wheel have increased our repair rates while reducing repair times. We focus on our members' and customers' needs at a breakdown and are introducing services to ensure a more personal response.
- › We are investing in additional patrols and in our call centres to improve our resilience and service levels. Our digital platform including our app will continue to improve the members' and customers' experience.
- › We believe that our investment in connected car, including Car Genie, will enable us to predict – and ultimately help to prevent – breakdowns, transforming the industry and helping members to manage their cars' conditions and costs.





Emerging trend Connected car

Original Equipment Manufacturers (OEMs) are increasingly including the capability of fault reporting in vehicles. Is there a risk therefore that the AA becomes disintermediated, lowering the demand for breakdown assistance service if OEMs' customers go direct to them?

Where we see the opportunity

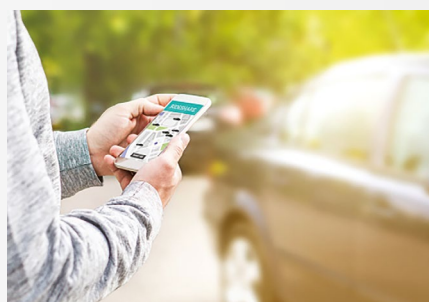
- › The AA will continue to proactively build relationships with OEMs, improving our offering so that we can continue to provide a critical service which they cannot provide themselves – we are trusted by more than 13 million car owners to deliver roadside assistance.
- › As we develop our connected car product, we are working closely with OEMs to ensure that they benefit from what we can offer. This includes technical support from our broad experience across the market and accessing their connected car feeds to be able to address faults that are better serviced by us. We believe our participation in connected car leads to an enhancement of the value the AA provides OEMs and that we can become a partner of choice for them.
- › Our experience since the launch of Car Genie in August 2017, demonstrates the potential to predict up to one third of breakdowns. Such digital products will, in combination with our app which is achieving significant engagement, create a powerful digital platform. The app has attracted interest from our B2B partners and we are exploring ways of sharing our digital products with them. We believe this approach will appeal strongly to younger customer segments and we also expect to be able to use telematics data to lower insurance premiums.

Emerging trend Electric vehicles

Electric vehicles (EVs) are more reliable and as their numbers increase, will the AA lose relevance?

Where we see the opportunity

- › Whilst EVs are more reliable than petrol and diesel cars, they still suffer from non-mechanical breakdowns including those related to tyres and batteries. Our experience is that EVs have greater wear and tear on tyres than traditional cars, due to their greater weight.
- › We will continue to invest in providing our patrols with the latest technology to enable them to diagnose and repair specific EV faults. Our exclusive partnership with Chargemaster, the biggest supplier of charging points in the UK, who are also the owners of the Polar card which is used for accessing these, gives us a significant competitive advantage in this market.

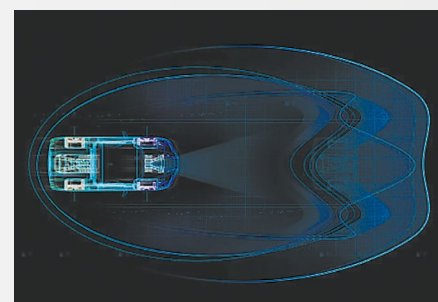


Emerging trend Car pooling

Car sharing via online platforms, either from professional operators or on a private, peer-to-peer basis, is becoming more popular. Could this lead to margin dilution as fewer consumer members take breakdown cover?

Where we see the opportunity

- › We have considerable experience in working in partnership with fleet and leasing companies. They value the services we provide to their customers and we will develop the specific services to cater for these markets.
- › At the same time, we are clarifying and enriching the benefits of being a personal member of the AA so we have a suitable proposition to maintain members under alternative ownership models.
- › We are looking at the opportunities for specific services for non-owner drivers where the benefit of membership is less vehicle-related and more personal.



Emerging trend Autonomous vehicles

The development of autonomous vehicles (AVs) is fuelled by expectations of safer travel. Are there concerns that this will lead to fewer breakdowns and lower levels of individual ownership, generating an eventual shift to the lower-margin B2B model?

Where we see the opportunity

- › We are encouraged by the growth of the AV market which represents another opportunity for innovation in our business, albeit far-off and subject to the removal of significant barriers. In the interim we will continue to engage positively with the industry, our business partners and Government to ensure we stay ahead of the technology. We expect this ultimately to offer additional services, including technical assistance, to realise additional revenue streams.





Market context

Developing scale in a competitive insurance landscape

Insurance has been an integral part of the AA since 1967. The insurance market has become highly competitive and we have lost our once dominant position in motor insurance broking. This is due to a combination of historic under-investment, a short-term focus on profitability, and the growth of PCWs.

Over the last 10 years the proportion of motor sales from PCWs has increased to 70%, driving competition based on price, ensuring only the most adept and agile businesses outperform. At the same time there has been regulatory change.

We have invested to increase our competitiveness, both in the creation of our in-house underwriter and in putting Insurance Hosted Pricing (IHP) technology into our panel. This has returned the broker's motor policy book to growth and we expect to use the same approach in our home insurance book.

Insurance is at the core of the membership proposition we are developing. Our new strategy focuses on how we offer more to our customers and accelerate growth. We believe the AA has the strengths and strategy to address the trends in the market and compete effectively.



Emerging trend

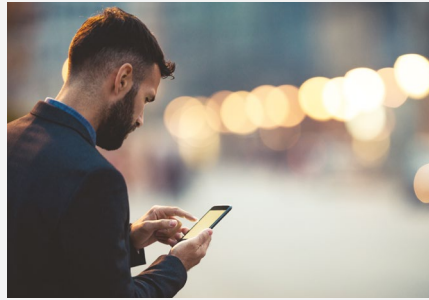
Claims and premium inflation

2017 was another year of price inflation across the market, driven by increasing claims costs and increases in Insurance Premium Tax (IPT). Are you worried about the impact of this on your business and plans for growth given the competitive nature of the market?

Where we see the opportunity

- › Price inflation drives churn which affects the whole market; however, as we are improving our price competitiveness and have plans to grow, this churn provides us with opportunity.
- › While our cost base is highly efficient, our plans factor in managing it as we grow.
- › The AA currently provides motor insurance for approximately 9% of its roadside members. Our investment in IHP for the brokers' panel members and the ability of our in-house underwriter to leverage our proprietary data on roadside members has already turned around our motor book and is expected to drive further growth both within the existing member base as well as through diversification into never-members.
- › We have now been underwriting home insurance for over a year and are now planning to improve our pricing capabilities through the implementation of IHP with some of our home panel members. Over the next few years, this investment is expected to arrest the decline in the home policy book and then return it to growth.





Emerging trend

Increasing application of technology

Can the AA participate in new technology which has the power to create feature-rich insurance apps and systems that can analyse vast amounts of data? Given the quantum of confidential information involved, is the AA putting more investment into cyber security?



Emerging trend

Increasing regulation and legislation

Insurance regulation has continued to evolve. How are you dealing with the risks? Do you envisage any limitations from the right to use data for profiling following the General Data Protection Regulation (GDPR) changes?



Emerging trend

Investment for scale

To develop scale and accelerate growth, additional investment will be required in technology and solvency capital. How can the AA grow its small share of the motor and home insurance markets?

Where we see the opportunity

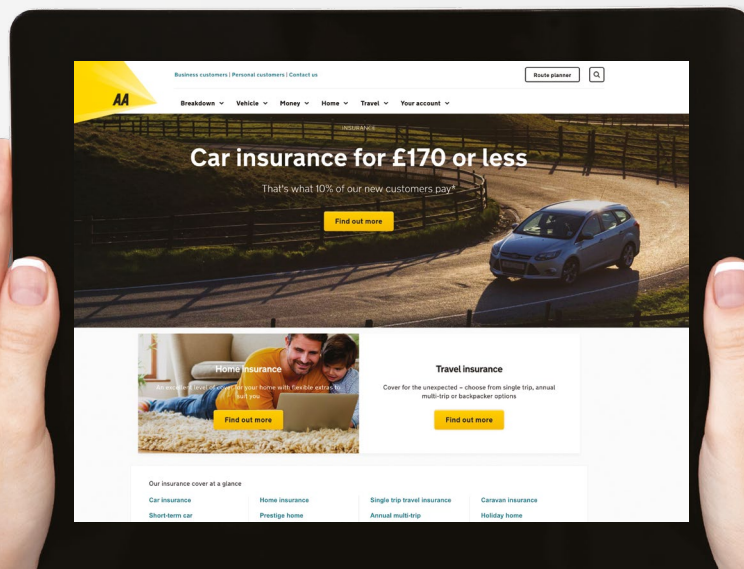
- › Our plans build on our leading brand consideration, valuable data and distribution platform. With our strong cash generation, we can continue to fund the additional levels of investment and policy acquisition costs required to grow the broker and the underwriter.
- › We have plans for systems investments within our own business to drive efficiency. Our plans to continue to put IHP into our panel members should improve our pricing agility and drive growth in future years.
- › In addition, we will grow the underwriter. This will require solvency capital of approximately £50m, half of which will be funded from internally generated cash, which is available, and half from the profits of the underwriter.
- › By ensuring our pricing agility through IHP, greater efficiency through better internal systems, and continued growth in our underwriter, we believe we can over time achieve a turnaround in the home book and accelerate growth in the motor book.

Where we see the opportunity

- › The AA is embracing this technological change and capitalising on our leading brand position. Our proprietary data on roadside members gives us a distinct advantage compared to other underwriters in respect of current members and ex-members. We share some of this data with our other panel members which supports the growth of our broker.
- › Additional investments in IHP as well as in connected car, will give us real-time pricing capabilities and additional data on the car and the driver to enable us to apply technology and price more competitively.
- › We are alert to the cyber security risks and managing them closely.

Where we see the opportunity

- › We continue to engage positively and proactively with the Financial Conduct Authority (FCA) and Government on the range of issues the insurance sector is dealing with.
- › On data protection, we are ensuring our position is robust and commercial in view of new GDPR legislation and have invested in people, including a new data protection officer, and technology to manage our risks better.
- › We are making sure marketing channels and permissions are used effectively without intrusion to our members. Many membership benefits are covered under the provision for legitimate interest allowing us to make members aware of related products and services deemed beneficial to them.



Chief Executive's strategic review

Unlocking the full potential of the AA



I believe that we can unlock the potential of this great company. With the right strategy, the right level of investment, the right leadership and the right culture we will put service back at the core of all we do, take full advantage of the data we have for the benefit of our customers, and innovate to take the business to the next level. This will deliver brilliant products and services for our customers and good returns for shareholders and bondholders.

Simon Breakwell
Chief Executive Officer



This year's financial performance is in line with the guidance we gave at the interim results in September 2017, despite challenging weather conditions. This was just seven weeks after I took over as Acting CEO and it was then that I took over as permanent CEO.

I immediately started from scratch to look at what I believed this business could deliver and what it would need to do so. This represented a very concentrated effort from the entire team and resulted in the strategy update on 21 February 2018.

Building on strong foundations

Our new strategy builds on two critical things, first the fundamental strengths of this business and its brand, and secondly, on the good work that has been done since the IPO.

Results in line with expectations

Trading Revenue grew 2% to £959m, driven principally by the strong performance of Insurance, both our Underwriter and Insurance broker, as well as Roadside. Driving Services, which is now within Roadside, was broadly flat. The performance is discussed in the business review on pages 24 to 25.

We are building on the strong fundamentals of the business

- › High recurring revenues and significant cash generation
- › A highly regarded and trusted commercial brand
- › Clear leadership in the stable roadside assistance market
- › High levels of retention and loyalty among our personal members
- › Strong market position in Roadside
- › High brand consideration in Insurance
- › An experienced and dedicated workforce

Trading EBITDA was £391m, in line with our guidance. The 3% decline compared to last year was due to the reduction in Roadside Trading EBITDA, reflecting the higher costs from third party garaging due to workload peaks and the higher number of breakdowns attended. The 8% increase in Insurance Trading EBITDA reflects the improved performance of both the underwriter and the broker. Head Office costs, which have now been allocated to segments, were flat during the year. Group Trading EBITDA margin reduced from 42.9% to 40.8% as a result of the lower profitability in Roadside.

Operating profit before exceptional items decreased by 4% to £304m, principally due to the reduction in Trading EBITDA and the increase in amortisation and depreciation reflecting the recent investment in transformation capital expenditure.

Exceptional operating items were lower at £3m income (2017: £32m cost), including £24m relating to business transformation costs and £27m impairment of goodwill offset by a £6m gain on the disposal of the home emergency services consumer business, a one-off pension past service credit of £34m from the restructuring of the UK pension scheme and a credit of £7m for the reversal of share-based payment charges for the former Executive Chairman, and a £9m improvement in onerous property provisions.



Operational headlines

A great deal has been done during the year and there is a lot to commend...



Following the launch of **Car Genie** in August, members currently have approximately 6,000 units. Our trial demonstrated that we can potentially predict up to one third of breakdowns.



We grew **new paid personal Roadside members** by 7% although overall numbers declined 1% to 3.29m. Retention was broadly flat at 82%, but we no longer benefit from the free-to-paid insurance channel.

Roadside B2B customers declined 1% as a result of the anticipated reduction in AVAs and the decline in new vehicle sales. However, breakdowns rose, increasing revenue under pay for use contracts. We have retained or extended contracts with five of our major accounts.

Basic earnings per share from continuing operations rose by 6.0p, from 12.2p to 18.2p mainly as a result of the pension past service credit. Adjusted basic earnings per share increased by 0.5p from 21.3p to 21.8p. The adjustments are explained further in the Financial Review on page 28.

Cash flow from continuing operating activities before exceptional items and taxation decreased from £371m to £368m. Capex included £34m of IT transformation capex, the final tranche of the investment originally set out at the IPO, and £53m of maintenance capex (including finance leases net of proceeds of sale of vehicles). Free cash flow before equity for continuing operations was an outflow of £5m (2017: inflow of £87m).

Strategy update – 21 February 2018

My strategic review included a comprehensive bottom-up analysis of every aspect of our business. My conclusion was that the AA is a phenomenal business and that we could build on our leading position in Roadside, our trusted brand and our highly-skilled and committed employees with a deeply embedded customer service ethos. All I saw strengthened my confidence about our ability to realise the opportunities and convinced me of the positive long-term outlook for the AA.

The objectives of the strategic plan are to deliver targeted investment in our people, our products, our systems and operations. We are building on the solid foundation that our investments since the IPO have created, and addressing the challenges we face.

This strategic plan will deliver front line resource to improve the efficiency, predictability and resilience of our Roadside operations as well as investment in game-changing growth drivers – Insurance and connected car. These investments, while reducing our short-term profitability, are vital to our long-term success. Our development in connected car – started with our Car Genie launch in August 2017 – could take the AA from being a service helping when you break down to one which potentially predicts when you might break down in the first place allowing scheduling of repairs and a great experience for customers.

I am confident the priorities we set out in February will transform our products and service offerings to our customers by creating a truly innovative and differentiated product proposition which will deliver long term shareholder value. Please find our full strategy update on pages 14 to 17.

Executive appointments

We have strengthened our Executive Committee with the appointment of Gareth Kirkwood and Ollie Holden. Read more on pages 54 to 55.

As Chief Customer Operations Officer, Gareth is responsible for ensuring we provide the highest standards of service to our customers from their first contact and then throughout their lifetime with the AA. Gareth's experience in customer facing operational roles in various British Airways divisions and within telecoms, marine and travel businesses gives him highly relevant expertise.

Chief Information Officer, Ollie is accountable for defining and implementing the IT strategy for the Group, shaping the digital transformation and providing robust IT services to customers and employees. Ollie has highly relevant experience in leading IT and change as a senior manager within Accenture, LV and TalkTalk.

We have also strengthened the teams below the Executive Committee and are rebuilding our culture to generate the high-performance behaviours needed to deliver the ambitions we have set.

Corporate responsibility

I have been very impressed by the ethos at the core of the AA. Our values do ring true when you see people do their jobs and there is a potent belief in the service we provide. However, we need to integrate this ethos into our operations more structurally to ensure the support and expertise is available to deliver the excellent service our members and customers deserve.

We conducted a wide ranging consultation with shareholders, among others, and we thank all participants. This has led to a change in our approach to CSR and we have a new CSR strategy. We will deliver this strategy over the next three years, aligning it with our overall strategy because it reinforces what makes the AA great. We will also ensure that our business partners and suppliers are aligned with our business ethics and commitments. This is covered fully in the CSR section on pages 38 to 49.

Pensions

In June 2017, we concluded the triennial review of the AA's UK defined benefit pension scheme and agreed a funding plan for the deficit which had increased, largely as a result of the reduction in long-term gilt yields. A nine-year plan of incremental funding is now in place, taking into account the continued funding of the previous deficit. The next triennial actuarial review is scheduled as at 31 March 2019.

Changes successfully made to the defined benefit pension scheme mitigated some of the recent increases in ongoing pension service costs. Overall, the changes have reduced our exposure to pension risks, increased our competitiveness within our industry, and provided for a more consistent pension offering across our business. This is covered in more detail in the Financial Review on page 31.

Refinancing

The refinancing in July 2017, which included the use of cash to repay £98m of the Senior Term Facility, further reduced the cost of borrowings and extended the average maturity of our debt with the first repayment due in July 2020. Since the IPO in June 2014 we will have reduced the annual debt interest cost on our borrowings by £90m excluding the hedging costs.

Outlook

The new strategy plans for additional investment to support the business and has resulted in a change in expectations for FY19 which we announced on 21 February 2018. We expect FY19 Trading EBITDA of between £335m and £345m. This provides a base upon which we can return to growth. We are targeting annual Trading EBITDA growth, of 5% to 8% from FY19 to FY23.

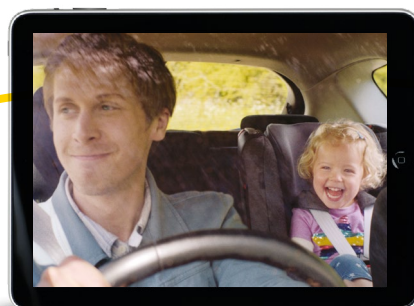
Despite the investments made up of capital and operational expenditure in FY19, we expect to generate free cash flow of approximately £20m even in this year. As this is the low point of cash generation, we expect to generate in excess of £80m of free cash flow in FY20 and in excess of £100m per annum thereafter, excluding the cost of any refinancing.



Simon Breakwell
CEO



We grew our **motor policy book** by 6% but overall motor and home policy numbers were flat at 1.4m as home policies continued to decline. The growth in the motor book was partly driven by the success of our in-house underwriter.



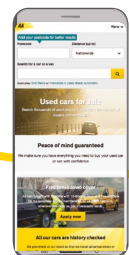
The **new advertising campaign** has been well received and driven a significant increase in awareness among our target segment.



Watch our latest advert here
theaa.com



Financial Services did well as our partnership with the Bank of Ireland continues to build momentum. Products are up 42% to 142,000 (2017: 100,000).



Since the year end, we completed the acquisition of **AA Cars**, an online second-hand car sales platform which we can integrate into our membership proposition, specifically around car finance.

Our strategy

Putting service, innovation and data at the heart of the AA

Strategic planning process

My first 150 days in the business

Our strategy

My strategic review included a comprehensive bottom-up analysis of every aspect of our business

Business review

A rigorous bottom-up review

Leadership refresh

Fresh talent brought in at Executive level

Employee engagement

Conducted our first survey

Product innovation

New team created

Tech and data audit

Initiated a full audit of our capabilities

Customers

Gaining greater and more extensive understanding

Insurance

Deep dive into our opportunities

ROADSIDE

Innovate and grow

OPERATIONAL
& SERVICE
EXCELLENCE

SERVICE,
INNOVATION
AND DATA
AT THE HEART
OF THE AA

INSURANCE

Invest to
accelerate growth

HIGH
PERFORMANCE
CULTURE



The conclusion of our strategy review was that the AA is a phenomenal business which could build on our leading position in Roadside, our trusted brand and our highly-skilled and committed employees with a deeply embedded customer service ethos. All I saw strengthened my confidence about our ability to realise the opportunities and convinced me of the positive long-term outlook for the AA.





1. Innovate and grow Roadside

Strategic update

We are putting service, innovation and data at the heart of the AA

The strategy builds on a strong base. Since the IPO, we have increased paid new membership by 23% and improved retention by 3 percentage points. Our service ethos and dispatch system are strong. The foundations of our digital development are in place and our core membership IT system is well advanced. Despite this, we have not been able to grow our membership in a sustained manner.

Connected car

We are uniquely positioned to play a central role in shaping the way the market reacts to emerging trends, such as Connected car, electric and hybrid vehicle growth and changing ownership models. We believe these present opportunities for the AA and are already advanced in our Connected car development. Our implementation will mean that we are not simply layering digital onto the organisation, but actively embedding it deeply into our product set and operations.

Connected car is expected to transform our Roadside offering by driving real benefits for customers as well as reducing costs. The AA's prognostic expertise and new products will enable us to move from reacting to breakdowns to predicting, preventing and protecting customers against them. Our trial and experience, since launch of Car Genie in August 2017, demonstrates the potential to predict up to one third of breakdowns. Such digital products will appeal strongly to younger customer segments and continue to strengthen already significant app engagement. They have also attracted significant interest from our B2B partners and we are exploring ways to leverage these products with them. During FY19, we will invest in rolling out Car Genie to tens of thousands more of our customers, allowing a larger-scale test of its impact on membership retention, operational benefits and distribution models. This will lead to the offering of a fully integrated, connected membership proposition. From FY20 we plan to extend the rollout to include B2B partners and connected insurance propositions, and to drive mass adoption. We believe we can reach scale with B2B partners from FY21.

Growing our base with younger segments

In addition to our traditional over 50 core demographic, we are now marketing to a younger base. We have already grown in younger customer segments over the past 12 months, but there is clear room for further growth in these under-penetrated segments. We will appeal to the needs of younger customers for a breakdown service to be simple, easy and digital through our innovative new products.

Digital adoption

Our breakdown app is highly successful and already over one third of our members have registered for it. The app simplifies the breakdown experience and 20% of consumer member breakdowns no longer involve a call as they are reported directly through the app or online. We will build on this to appeal to new customer segments and engage them in our app as a portal to a wider set of services and benefits, while reducing call centre costs.

The app is crucial to making the AA more relevant in the lives of our members and driving loyalty through membership benefits. Our app engagement programme is designed to expand the number of users who log in regularly and grow the number of users of our member services and benefits programme from its current level of more than 100,000 per month.

Membership systems investment to drive retention

We will invest in new systems to strengthen membership retention, increasing the sophistication of our retention activities. This will include the full implementation of the brand new membership IT system, including the Customer Relationship Management (CRM) system. Our 'Stay AA' reactive customer retention proposition continues to be effective, with an all-time high save rate of 72%, up from 57% at launch in 2014, and a discount rate at an all-time low of 22%, down from 35% at launch. We believe these actions can continue to increase retention.



We are building on the good work done since the IPO...

› Retained 100% of major B2B accounts and won VWG and LexAuto Lease



› Grew paid new members by 23%



› Increased online sales by more than 1/3rd



Our strategy

continued

2. Accelerate growth in Insurance

The AA's Insurance business has fundamental strengths and we have a significant opportunity to accelerate growth over the next five years. Progress to date has been excellent, particularly in returning the motor book to growth, but we believe that with further investment in both our broker's pricing agility and our underwriter, we can accelerate that growth.

We have significant scope to sell insurance to Roadside members (only 9% of our 3.3m base have AA motor insurance) as well as non-members (whom we have not targeted in the past). We will build on our brand consideration, which is the highest in motor insurance, and our valuable data and analytics. Growing the underwriter will require solvency capital, half of which we can fund from the profits of the underwriter. A further £20m to £25m will be funded from PLC resources.

While additional growth is expected to result in a short-term negative impact on EBITDA, it will help deliver long-term growth. We are targeting c2m motor and home policies by FY23 and strong growth in profitability.

Broaden footprint to include non-members and younger customers

We will target greater market share and growth from broadening beyond our narrow customer base. In our underwriter, we are currently focused on 30-year plus members and former members, but we will expand our proposition to underwrite non-members, including younger customer segments. This will also promote opportunities to cross-sell Roadside membership.

Driving more competitive premiums

Since its launch two years ago, the underwriter has grown rapidly by using our proprietary data to drive more competitive premiums and, in its first year, bringing in a majority of customers who were new to AA Insurance. We will also continue to invest in IHP, which enhances our broker's pricing agility, and improve our data analytics. This investment will allow us to create bespoke pricing and unique insurance products for customers which more accurately meet their needs.

Digital and connected car offers

We expect to benefit from using the data collected from Car Genie, and other connected car products, prior to pricing and insuring customers, allowing for compelling telematics economics.

The integration of our digital and connected car products and data across our Roadside and Insurance businesses will enable a leading customer offering through its simplicity and as a straightforward, one-stop-shop for motoring needs.

We believe connected car offerings will unlock new propositions for younger, more digitally-focused drivers. The Driving School also gives us strong positioning with younger driver segments, reaching c80,000 customers per year.

3. Operational and service excellence

Building resilience into our operations and service will enable us to achieve more consistent service delivery

We plan to improve customer service at peaks in demand and decrease our reliance on third-party garaging. We believe that investment in the front line, including additional patrols and call centre agents, will give us the resilience we need to achieve consistent service levels. In addition, our new leadership team is conducting a management restructuring and has plans to improve efficiency. In addition, we are reviewing ancillary sales performance.

The measures to be undertaken in FY19, will build a more resilient base for improving both service and cost with the following targets:

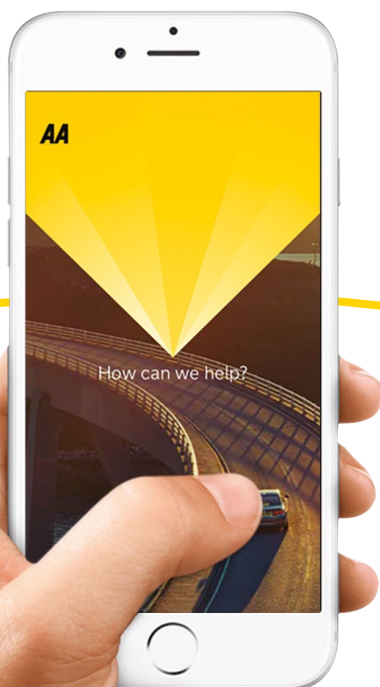
- > Absorb inflation in FY20 and FY21
- > Improve consistency of call-to-arrive times to 45 minutes
- > Increase consistency in call handling, answering 80% of calls in 20 seconds
- > Achieve 10% growth in ancillary sales

4. Create a high-performance culture

Driving a culture of high performance will be critical to realising our strategy because our people are a key enabler of our business

Our three-year planning process will focus on delivery, clear accountabilities and embedding operational improvements. Key drivers will be greater agility and improved listening and engagement.

> 1/3rd of members registered for the app and approximately 29% now use it in a breakdown



> Launched our in-house Underwriter

The financial implications of the strategy

As a result of the new strategy, FY19 Trading EBITDA is expected to be between £335m and £345m. We expect a net impact from a decline in Roadside revenue on Trading EBITDA of c£12m. This reflects a marginal decline in memberships and business customers and the IPT increase of June 2017. Growth in the insurance motor book is expected to contribute £9m to Trading EBITDA.

Our planned investments are expected to amount to £26m of additional operational expenditure in FY19. We will invest £15m across all initiatives in Roadside, including operations, enhancements to the digital platform and connected car. Growth in our Insurance portfolio is expected to result in lower short-term profitability in FY19 and incremental operating costs of c£10m.

Strategic projects are expected to generate EBITDA of £6m this year. These largely relate to the acquisition of AA Cars, in which we held a 50% profit share, and the disposal of our Home Emergency Services consumer business which we had previously announced.

Additional central and people costs, net of savings, and additional pension charges, following last year's triennial review, are expected to lower Trading EBITDA by £12m.

Growth projections to FY23

From the base in FY19, we expect to grow revenue and Trading EBITDA to FY23. The benefits of the investment in Connected Car are not included in these estimates.

Capex guidance

IT transformation

As indicated at the interim results, we expect the balance of the original IT transformation programme to cost an additional £35m, with £31m incurred in FY19 and the balance of £4m in FY20. The last leg of the IT transformation relates to the roll-out of the membership system and CRM to our existing members, which has now commenced.

Growth capital expenditure

Capital expenditure of £19m relates to the investment required to position the AA for growth from FY19. This includes the enhancement of our Roadside digital capability, additional investment in IHP and new systems to support the growth of the underwriter. It also includes our planned investment in Connected Car of c£7m per year over the next three years.

Maintenance capital expenditure

We expect maintenance capital expenditure (including finance lease payments net of proceeds from disposal of fixed assets) to be stable at £55m over the next three years. This includes additional IT maintenance spend given the increased sophistication and scale of our requirements.

Strong free cash flow normalising after low point in FY19

Factoring in the lower EBITDA and additional growth capex in FY19, we expect free cash flow to equity this year to be c£20m. Adjusting for the one-off impacts in FY19, our normalised free cash flow to equity would be in excess of £100m.

Following the low point in FY19, we are confident that we can deliver free cash flow to equity in excess of £80m in FY20 and in excess of £100m from FY21, excluding the cost of refinancing.

Having created a more resilient base from which to grow profits and with normalised levels of capex, we believe we will be in a position to deliver this.

The strength of our debt structure

We remain well funded to meet all of our operational and debt financing requirements. The combination of our WBS debt structure, our successive refinancings and our strong cash generative business model give us the following attributes:

- › The average cost of debt, at 4.52%, is significantly lower now than it was at IPO
- › The average maturity of our debt is just over 4.5 years
- › We have significant headroom above our financial covenants, which are not linked to leverage. Trading EBITDA would have to fall to c.£200m, for us to be close to breaching our default covenants
- › The WBS is flexible from an operational perspective and its credit enhancing characteristics enable refinancing at attractive rates
- › Long-dated bonds paying fixed interest rates and pricing reflecting the investment grade of the A notes
- › We pay a lower debt service charge than we would with a traditional bank facility as a result of the lack of amortisation on debt payments

Conclusion

The strategic plan will unlock the AA's potential by fundamentally transforming the way we support our customers through a differentiated product proposition. This will enable us to innovate and grow Roadside and accelerate growth in Insurance, securing a better future for the AA, our members, customers, employees and investors.



- › Reversed the decline in motor Insurance
- › Improved patrol service levels



- › Increased loyalty with retention at 82% from 79% at IPO



- › Created connected car JV and launched Car Genie
- › Invested in core dispatching and membership systems



- › Reduced the annual debt interest cost on our borrowings by £90m excluding the hedging costs

Q&A

Shareholders' questions, Simon Breakwell's answers.



Q. What did you see in the AA to make you take the job?

A. What shone out and convinced me to take the job was the amazing commitment of our patrols, our call centre agents and all our people who are focused on "being the AA" and delivering services which are so highly valued.

I am also convinced that there is an opportunity here to do something great in bringing this business into the modern world and transform the way we operate. My experience in tech tells me we can do it, but it also warns me of the importance of engineering it into the foundations of the Company. I see a real ambition within the AA to achieve this. By way of a reminder, this is not some blue-sky scenario – our connected car thinking is based on the success of Car Genie and, more importantly, while the costs are factored into our thinking, the upside is not.

READ MORE: CHIEF EXECUTIVE'S STRATEGIC REVIEW P12

Q. The new strategy feels very similar to the old strategy which has not yet delivered. What is the difference?

A. The new strategy represents an evolution on the achievements over the last three years, since the IPO. These investments were essential and have delivered very positive benefits. But now we need to do more and go further to drive that long-promised predictable growth which the previous plan had not yet done.

A key difference will be execution – my team is utterly pragmatic and they are focused on what it takes to meet the targets we have set out together.

READ MORE: PUTTING SERVICE, INNOVATION AND DATA AT THE HEART OF THE AA P14

Q. There are a lot of changes in the automotive market. Is this a market in structural decline?

A. This is absolutely not a market in structural decline. Quite the opposite.

Demand for our service has grown in the last couple of years and our data shows car ownership has been increasing overall, except in London. We have increased new members, loyalty has gone up and, as a result, we have slowed the decline in our membership base since the IPO.

On the B2B side, our partners are excited by our new ideas to develop and enrich the service we give them.

We are really excited about the opportunities the emerging trends bring. Although the numbers are still small, electric vehicles (EVs) are with us and the need for our service will change but not go away – for example, EVs' heavier wear and tear on tyres results in more callouts. I am convinced by our ability to innovate – we have dealt with pretty massive changes in mechanics, technology and ownership since 1905! Just think of the traction we have achieved with our app.

READ MORE: OUR MARKET CONTEXT P8


Q. You talk about long term-targets for FY23. Do you have any shorter-term milestones to measure success?

A. As you can imagine, there is no shortage of goals, but the key ones for FY21 are as follows:

- › We expect to have returned Roadside membership to growth
- › Insurance policies overall will be growing – motor already is, but home should also be growing by then
- › We will be managing costs better. With greater resilience, we expect by then to be absorbing the cost of inflation


Q. Does your large amount of debt affect the business and what can you do to reduce it?

A. Our leverage does not restrict us operationally. The best demonstration of this is that in our FY19 plans, our very considerable investment in growth means we reach a low point of EBITDA and yet we remain cash positive. This business generates a huge amount of cash. When we are no longer diverting it to invest in the business, we will use it to pay down debt. Reducing debt will take a while, but in the meantime our plans enable us to grow EBITDA and bring leverage down that way.

 READ MORE: FINANCIAL REVIEW **P27**

Q. Why not cut dividend payments altogether instead of paying 2p per share per year?

A. We have decided to keep an annual dividend payment because we can afford to. We expect to generate sufficient excess cash flow to finance operations, invest in growth, cover debt payments and pay a modest dividend.

 READ MORE: FINANCIAL REVIEW **P27**

Q. Isn't insurance a fundamentally competitive market in which you are a small player? Why are you convinced you can grow?

A. It's worth remembering that we are growing already – we have turned around our motor book and we believe we can turn around our home book too.

We have unique strengths which we haven't to date maximised in our insurance business. We have a trusted brand – the highest brand consideration in motor insurance – excellent customer data and a good distribution platform. This will allow us to broaden our underwriter footprint including testing the market for younger drivers, drive more competitive premiums using our data, and we're going to innovate, for example, using our telematics to offer our customers a better experience when it comes to buying insurance. A lot of the ground-work – investment in systems and people – is already in place in our broker and our underwriter.


 READ MORE: OUR MARKET CONTEXT **P8**

Q. Why is your connected car offering better than the manufacturers'? What do you bring that they don't?

A. We are an ideal partner for manufacturers – we are not looking to compete with them.

With our European Roadside Assistance partners, we have access to more vehicles and telematics data than they do, which means we are in a uniquely better position to predict and ultimately prevent breakdowns than they are. To act on data predicting a breakdown, you have to have excellent systems that can trigger out-bound calls or texts really quickly. This is a difficult capability to build and something we are much better set up to do. We don't believe that the manufacturers want to get into breakdown, with all the barriers they would have to surmount. We can offer this service to them.

We will be launching a fully-costed trial which will give us more clarity on what this opportunity could look like. Only when we are sure, will we factor in any upside.

 READ MORE: PUTTING SERVICE, INNOVATION AND DATA AT THE HEART OF THE AA **P14**

Q. What has the App given you?

A. The App has achieved real traction among members, which is increasing their stickiness. A third of our members are registered.

On a more practical front, members, who are currently eligible for the App, represent about half our breakdowns. 20% of them are now reporting and tracking breakdowns through our app and online. Another 10-15% call in but then track their patrol as they head to them on the App or online which cuts calls. The App has reduced calls for these breakdowns by just over 30% – a big impact on our call centres.

Q. How are you going to manage the costs of your operations better?

A. We are investing to improve our operational resilience. On the vast majority of days in the year we provide excellent customer service. However, during periods of extreme weather – hot, wet or cold – we have not always been able to provide the service we pride ourselves on as we are forced to use third party garaging. The investment we are making in patrols will help us to deliver better service on these challenging days.

Our employees

The people making a difference for our customers

The AA's people are its life blood and we acknowledge and thank them for their enormous commitment and sheer hard work. At our Employee Awards every year we celebrate these qualities and the dedication to our values. In 2017, we had 20 awards and 96 finalists. We have a selection here but we honour all those involved and congratulate the winners.



AA award winners 2017

Patrol Vince Crane

Recovery Patrol Brent Pugh

Assist Technician Ben Chance

Jaguar Land Rover Dedicated Technician Cihan Gulesin

Volkswagen Group Dedicated Technician Paul Gillett

Contractor Award Alan Graham, Recovery Services

Direct Sales Force Agent Chris Spain

Home Services Engineer Paul Allen

Motoring Services Award Richard Sanders

Driving School Award Wyn James

Road & Home Call Centre Customer Adviser Edward McIlwaine

Sales & Service Call Centre Customer Advisor Chloe Arnett

Insurance Call Centre Customer Adviser Victoria Waters

Call Centre Team Leader Matthew Barton

Digital Hero Andy Leiper & Stuart Wingrove

Business Transformation Hero Alison Isaac

Support Expert Rebecca Hale

Leadership Award Caroline Jackson

Spirit of the AA – in honour of Di Kirman Nigel Hawkins

Brand Values Award Jason O'Keefe



Recovery Patrol of the Year

This award recognises the commitment to the brand and dedication of our recovery patrols. They are needed when vehicles have to be trucked away and cannot be towed by patrol vans or fixed at the roadside.



This is a fantastic job. Every day is different, not knowing where your next job is or who you're going to meet and seeing smiles on members' faces when you turn up is amazing. At the end of the day you feel you've achieved something and made someone's day better.

Brent Pugh, Recovery Patrol of the Year



Patrol of the Year

This award recognises the patrol's skills, abilities and their dedication to the AA. The winner will represent the AA in a variety of ways over the next 12 months from his AA van with its special number plate of 999AA which is his for the year. Vince Crane (third left) receives his number plate from last year's Patrol of the Year, John Snowling (second left).



Working for the AA isn't just a job. I feel I represent the brand and the years of heritage and trust behind it and that I have to deliver excellent service every time through sun, rain or snow. Being given the opportunity to be at the forefront of this amazing service representing the best of the AA for a year means everything to me.

Vince Crane, Patrol of the Year



Support Expert award

The Support Expert award recognises individuals who provide an excellent service to their colleagues. They are recognised for consistent and outstanding performance, often working outside their area of expertise, to support their colleagues' needs.



The various roles I've had since I joined the AA at 17 have taught me so much and now I am trusted to support others. It could be our emergency breakdown systems, working with call agents or making our customers' experiences easier – it's all part of my role and I just love being in the thick of it!

Rebecca Hale, Product Owner – Reporting & Tracking Breakdowns Online



Digital Hero award

This award recognises individuals who have gone above and beyond the norm, significantly contributing to the delivery of our digital transformation programme.



We have delivered so much – the digital transformation has been phenomenal. We are very excited that Simon has real understanding of this side of the business and we believe that what we do has the ability to transform the AA. I am very proud to have been given this award.

Stuart Wingrove, Senior IT Developer



Sales & Service Call Centre Customer Adviser award

This award recognises the Customer Adviser from our Sales and Service call centres who has demonstrated consistently excellent performance standards. This involves having a sound knowledge of our products and services and offering top quality of service every time.



The award was great and I couldn't be more proud, but the thing is, I just love what I do. People are lovely – at least most of them – and I am just so pleased when I can help them. This is a great company, people know what they can expect from us and most of our customers are happy to talk to us.

Chloe Arnett, Customer Adviser



Spirit of the AA award

This award is in honour of the late Di Kirman a much-loved colleague. It recognises those who are held up by their peers and colleagues as embodying everything which is great about the AA. They constantly demonstrate the values we hold dear and will regularly go the extra mile for members and colleagues.



Being given this award was one of the proudest moments of my life and, in my case, it came after returning to work after a serious illness and meant even more. To be nominated by colleagues whom you respect and admire is fantastic, but what keeps me going is the pride of working for the AA and helping our members in their hour of need.

Nigel Hawkins, Recovery Patrol



Insurance Call Centre Customer Adviser award

This award recognises the customer adviser from our Insurance call centres who has performed at the highest level, displayed a sound knowledge of products and services, and ensured the best quality of service is offered to our customers.



The thing I love about my job is that I know I can make the whole process of getting insurance easy and a pleasure for our customers. If I do it well, they get the insurance cover they need but also go away happy with the experience and their contact with me.

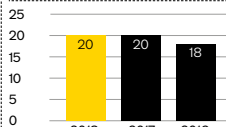
Victoria Waters, Customer Adviser

Key performance indicators

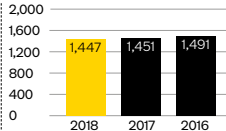
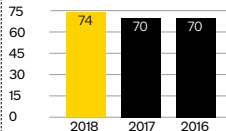
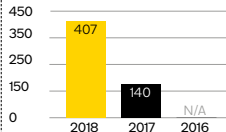
Our key performance indicators (KPIs) reflect the AA's strong fundamental characteristics which will deliver the strategy outlined on pages 14 to 17. The KPIs below reflect these fundamental characteristics and the performance underlying these KPIs is explained in 'Our Performance' and the 'Financial Review'.

Changes to KPIs this year: We have updated our KPIs to measure more accurately the impact of our new strategy. We have removed total shareholder return since IPO as this is no longer the sole component of Executive Directors' long term incentivisation. Insurance policies and average income per policy have been restated to show motor and home policies only.

Roadside

Strategic objective	KPI	Definition			Executive Directors' Remuneration						
Innovate and grow Roadside	› Paid personal members (thousands)	› Number of personal members excluding free memberships at the period end	3.3m -1.4%	 <table><thead><tr><th>2018</th><th>2017</th><th>2016</th></tr></thead><tbody><tr><td>3,289</td><td>3,335</td><td>3,331</td></tr></tbody></table>	2018	2017	2016	3,289	3,335	3,331	Proposed PSP performance criteria ² Individual objective for bonus of CEO
	2018	2017	2016								
	3,289	3,335	3,331								
	› Business customers (thousands)	› Number of business customers at the period end	9.9m -0.5%	 <table><thead><tr><th>2018</th><th>2017</th><th>2016</th></tr></thead><tbody><tr><td>9,928</td><td>9,976</td><td>10,216</td></tr></tbody></table>	2018	2017	2016	9,928	9,976	10,216	
	2018	2017	2016								
9,928	9,976	10,216									
› Average income (£)	› Average income per personal member excluding free memberships	£157 -0.6%	 <table><thead><tr><th>2018</th><th>2017</th><th>2016</th></tr></thead><tbody><tr><td>157</td><td>158</td><td>156</td></tr></tbody></table>	2018	2017	2016	157	158	156	Proposed PSP performance criteria ² Individual objective for bonus of CEO	
2018	2017	2016									
157	158	156									
	› Average income per business customer	£20 0.0%	 <table><thead><tr><th>2018</th><th>2017</th><th>2016</th></tr></thead><tbody><tr><td>20</td><td>20</td><td>18</td></tr></tbody></table>	2018	2017	2016	20	20	18		
2018	2017	2016									
20	20	18									
	› Franchised driving instructors	› Number of driving school instructors at the period end	2,742 +5.2%	 <table><thead><tr><th>2018</th><th>2017</th><th>2016</th></tr></thead><tbody><tr><td>2,742</td><td>2,607</td><td>2,574</td></tr></tbody></table>	2018	2017	2016	2,742	2,607	2,574	
2018	2017	2016									
2,742	2,607	2,574									

Insurance

Strategic objective	KPI	Definition			Executive Directors' Remuneration								
Accelerate growth in Insurance	› Insurance policies (thousands) ¹	› Total motor and home policies sold in the last 12 months by our insurance broker	1,447k -0.3%	 <table><thead><tr><th>Year</th><th>2018</th><th>2017</th><th>2016</th></tr></thead><tbody><tr><td>Value</td><td>1,447</td><td>1,451</td><td>1,491</td></tr></tbody></table>	Year	2018	2017	2016	Value	1,447	1,451	1,491	Proposed PSP performance criteria ² Growth of insurance is an individual objective for bonus of CEO and CFO
	Year	2018	2017	2016									
	Value	1,447	1,451	1,491									
› Average income ¹	› Average income per insurance policy for motor and home	£74 +5.7%	 <table><thead><tr><th>Year</th><th>2018</th><th>2017</th><th>2016</th></tr></thead><tbody><tr><td>Value</td><td>74</td><td>70</td><td>70</td></tr></tbody></table>	Year	2018	2017	2016	Value	74	70	70		
Year	2018	2017	2016										
Value	74	70	70										
› Underwritten insurance policies (thousands)	› Total motor and home policies sold in the last 12 months by our in-house insurance underwriter	407k 191%	 <table><thead><tr><th>Year</th><th>2018</th><th>2017</th><th>2016</th></tr></thead><tbody><tr><td>Value</td><td>407</td><td>140</td><td>N/A</td></tr></tbody></table>	Year	2018	2017	2016	Value	407	140	N/A		
Year	2018	2017	2016										
Value	407	140	N/A										

1 Prior year figures restated to show motor and home policies only.

2 Subject to consultation with shareholders.

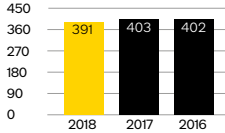
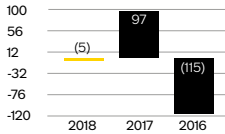
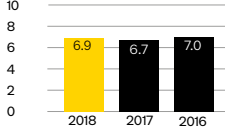
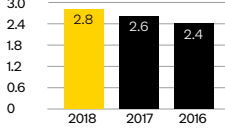
Operational and service excellence



Strategic objective	KPI	Definition			Executive Directors' Remuneration				
Build resilience into operations and service	› Breakdowns attended (thousands)	› Number of breakdowns attended	3.7m +1.2%						
				<table><tr><th>Year</th><th>Breakdowns attended (thousands)</th></tr><tr><td>2018</td><td>3,679</td></tr><tr><td>2017</td><td>3,635</td></tr><tr><td>2016</td><td>3,459</td></tr></table>	Year	Breakdowns attended (thousands)	2018	3,679	2017
Year	Breakdowns attended (thousands)								
2018	3,679								
2017	3,635								
2016	3,459								

Financial and other



Strategic objective	KPI	Definition			Executive Directors' Remuneration								
Grow profitability and cashflow generation	› Trading EBITDA (£ millions)	› Trading EBITDA is the performance measure most closely aligned to that required by our debt documents and is defined as earnings before interest, tax, depreciation and amortisation and excluding exceptional items, share-based payments, pension service charge adjustment and discontinued operations	£391m -3.0%	 <table><tr><th>Year</th><th>Trading EBITDA (£ millions)</th></tr><tr><td>2018</td><td>391</td></tr><tr><td>2017</td><td>403</td></tr><tr><td>2016</td><td>402</td></tr></table>	Year	Trading EBITDA (£ millions)	2018	391	2017	403	2016	402	Proposed PSP performance criteria ² Annual cash bonus – at least 50% based on Trading EBITDA. Remaining balance subject to Trading EBITDA adjustment
	Year	Trading EBITDA (£ millions)											
2018	391												
2017	403												
2016	402												
	› Free cashflow before equity (£ millions)	› Net cashflow before payments of dividends to equity shareholders	(£5m) -105%	 <table><tr><th>Year</th><th>Free cashflow before equity (£ millions)</th></tr><tr><td>2018</td><td>(5)</td></tr><tr><td>2017</td><td>97</td></tr><tr><td>2016</td><td>(115)</td></tr></table>	Year	Free cashflow before equity (£ millions)	2018	(5)	2017	97	2016	(115)	
Year	Free cashflow before equity (£ millions)												
2018	(5)												
2017	97												
2016	(115)												
Reduce borrowings and associated interest costs	› Leverage	› Ratio of net debt to Trading EBITDA for continuing operations for the last 12 months (see note 28)	6.9x -3.0%	 <table><tr><th>Year</th><th>Leverage</th></tr><tr><td>2018</td><td>6.9</td></tr><tr><td>2017</td><td>6.7</td></tr><tr><td>2016</td><td>7.0</td></tr></table>	Year	Leverage	2018	6.9	2017	6.7	2016	7.0	Proposed PSP performance criteria ² Individual objective for bonus for CFO
	Year	Leverage											
2018	6.9												
2017	6.7												
2016	7.0												
	› Interest cover	› Trading EBITDA divided by total ongoing cash finance costs (see note 6)	2.8x +7.7%	 <table><tr><th>Year</th><th>Interest cover</th></tr><tr><td>2018</td><td>2.8</td></tr><tr><td>2017</td><td>2.6</td></tr><tr><td>2016</td><td>2.4</td></tr></table>	Year	Interest cover	2018	2.8	2017	2.6	2016	2.4	Proposed PSP performance criteria ² Individual objective for bonus for CFO
Year	Interest cover												
2018	2.8												
2017	2.6												
2016	2.4												

Our performance

In line with the focus of our new strategy, we are reporting Roadside Assistance and Driving Services as Roadside and Insurance Services, including Financial Services, and the in-house underwriter as Insurance. We have also allocated head office costs to these divisions. A reconciliation of the old and the new reporting bases is on page 26.

Roadside



Trading Revenue

£814m

(£809m)

Trading EBITDA

£320m

(£337m)

Trading EBITDA margin

39.3%

(41.7%)

Roadside Assistance performance is driven by our personal membership base and supported by our business customer (B2B) base, underpinning the scale of our operations which is critical to our success. Each provide approximately half the jobs for the 2,900-strong patrol force. The growth in revenue despite the pressures on retention, reflected the fundamental strengths of the business, while reduced profitability reflected the challenges we believe our new strategy can counter.

The improved profitability of Driving Services is encouraging. We have 2,742 driving instructors in our franchised driving schools, the AA and BSM, providing driving lessons for approximately 80,000 learners each year. DriveTech is joint market leader in providing speed awareness courses for police forces in the UK and fleet training services.

results, retaining 72% of those who call to cancel, with discounts averaging 22%, compared with 57% and 35% respectively when the programme was launched in 2014. The discontinuation of the free-to-paid insurance channel from December 2015 has resulted in a reduction in membership by approximately 70,000 in FY18 and this pipeline of additional paid members has now ceased.

Average income per paid member declined 1% to £157 (2017: +1% to £158), reflecting our constraint in passing through price rises above the increase in IPT and the dilution of introductory discounts from the increased number of new members.

Business customers declined 1%, falling to 9.9m reflecting the anticipated decline in the number of Added Value Accounts (AVAs) with our banking partners Lloyds Banking Group and TSB and the lower number of new cars sales for our manufacturing partners. During the year we retained or extended a number of contracts including VW Group and Ford.

Average income per business member was flat at £20.

Trading EBITDA fell by £20m to £345m. Apart from the decline in membership numbers and business customers, this was largely the result of the increased costs of third-party garaging due to workload peaks and wage inflation which we were unable to absorb through price rises. Trading EBITDA margin declined from 49.2% to 46.2%.

Driving Services

Trading Revenue was flat, at £67m. The 5% rise in driving instructor franchises to 2,742 (2017: 2,607) was the result of improvements to our franchise proposition and the strength of the AA and BSM brands. This offset the marginal decline from fewer courses delivered by DriveTech. While the number of speed awareness courses for the police increased, the number of courses for our corporate partners declined.

Trading EBITDA rose £2m to £22m driven by the improvement in Driving Schools and efficiency savings in both businesses. Trading EBITDA margin rose from 29.9% to 32.8%.

Breakdowns attended

3.7m
(3.6m)

Paid personal members

3.29m
(3.34m)

Average income per paid member

£157
(£158)

Business customers

9.93m
(9.98m)

Average income per business customer

£20
(£20)

Driving instructors

2,742
(2,607)

Roadside

Trading Revenue grew 1% to £814m driven largely by increased pay-for-use B2B revenue. Trading EBITDA declined by 5% to £320m primarily reflecting the cost increases of service delivery. Head office costs declined from £48m to £47m. Trading EBITDA margin decreased from 41.7% to 39.3% reflecting the EBITDA decline.

Roadside Assistance

The contribution from Roadside Assistance rose 1% to £747m despite a decline in memberships and business customers. Growth was the result of increased pay-for-use revenue from B2B, increased ancillary sales and increased revenue from vehicle inspections, AA Cars and publishing.

Paid personal memberships declined 1% to 3.29m. New member growth of 7% (2017: 14%) was good, particularly against last year's strong performance, driven again by digital sales. Our expansion into younger segments has begun, helped by our effective and well-received "singing baby" advertising campaign. Retention was broadly flat at 82%, a strong performance given the significant challenges we faced. These included the impact of the rise in IPT in June 2017; the dilution from an increase in new members, whom we retain at lower rates; our completed programme of redress for customers affected by duplicate cover; and the introduction in April of new renewal price transparency regulations. StayAA, our proactive retention programme, achieved all-time high

Insurance



Trading Revenue

£145m

(£131m)

Trading EBITDA

£71m

(£66m)

Trading EBITDA margin

49.0%

(50.4%)

Policy numbers

Broker	Underwriter
1.4m (1.5m)	407,000 (140,000)

Motor policies

Broker	Underwriter
629,000 (594,000)	223,000 (115,000)

Home policies

Broker	Underwriter
818,000 (857,000)	184,000 (25,000)

Average income per policy

(Motor and Home policies only)

Broker
£74 (£70)

Financial Services products

142,000 (100,000)

The growth was driven by our insurance broker which has focused on the core products of motor and home insurance and returned our broker motor book to growth while slowing the anticipated decline in home policies. While our leading brand consideration in motor insurance has underpinned this strong performance, our in-house underwriter has been critical through its competitive pricing, as have investments in Insurer Hosted Pricing (IHP) to improve our pricing agility with our panel.

Our in-house underwriter's motor book was launched in January 2016 and followed in August 2016 with the launch of home policies. The underwriter's ability to price members' policies competitively is based on our extensive data. It is now in profit and has plans to extend beyond members.

Our financial services partnership with the Bank of Ireland, launched in July 2015, builds on a long past history of AA financial services and enables us to enhance our membership proposition.

Insurance

Trading Revenue rose 11% to £145m as higher revenue from our motor insurance broking, the growth in our in-house underwriter more than offset the lower revenues from the Home Emergency Services consumer business, which was sold in January 2018. Trading EBITDA rose 8% to £71m with flat head office costs of £9m. Trading EBITDA margin declined from 50.4% to 49.0% as a result of the increase in the lower-margin underwriter revenue.

Insurance Services (including broking, Financial Services and Home Emergency Services)

Trading Revenue rose 2% to £133m. We grew our motor book by 6% to 629,000 policies, benefiting from incremental sales and renewals through our in-house underwriter, which continues to perform ahead of expectations. We did well to achieve stable retention despite the challenges of the new renewal pricing transparency regulations from April; the impact of the Ogden rate change on cost of premiums, therefore driving churn and the IPT increases. We benefitted from improved pricing agility following the installation of IHP with five of our motor panel members, including our underwriter. This has enabled us to price more competitively and convert a greater proportion of quotes on PCWs.

In line with expectations, home policies fell 5% to 818,000 as we have not yet made the investment in IHP to improve pricing agility. Overall policy numbers are down as we continue to retreat from less profitable business lines, including insurance categories such as weddings and pets. Home Emergency Services policies for emergency repairs to boilers, heating systems and other domestic installations were down year-on-year. The sale of our Home Emergency Services consumer book was completed in January 2018.

The focus on greater profitability has driven average income per motor and home policy up 6% to £74 (2017: £70).

Financial Services revenue is broadly flat at approximately £8m. By the end of January 2018, we had 142,000 Financial Services products across our credit cards, personal loans and savings portfolio. This represents a balance sheet of

approximately £400m, broadly match-funded by deposits. Our partnership with the Bank of Ireland continues to build positive momentum on the strength of our brand and marketing expertise and Bank of Ireland's operational excellence. The AA membership base and brand are benefitting the business with over 17% of the non-ISA savings books held by members and 39% of our personal loans being written for vehicles. The completion of the acquisition of 100% of the AA Cars platform will enable us to expand our loan offering into the growing used car market.

Trading EBITDA rose 4% to £79m as a result of the growth of the motor book, the focus on the more profitable business lines and disciplined cost management. Trading EBITDA margin was higher at 59.4% (2017: 58.0%).

Insurance underwriting

Trading Revenue for our underwriting business was £12m compared to nil in the prior year. Gross earned premiums before our 80% reinsurance were £38m (2017: £10m). Deferral of broker commissions amounted to a reduction in revenue of £1m (2017: £3m). Trading Revenue is reported after accounting for the broker deferral adjustment, where the broker commission and associated acquisition costs are recognised over the life of the policy along with the underwriter premium.

We nearly doubled the motor book to 223,000 policies (2017: 115,000) and grew the home book very substantially in its first full year to 184,000 policies (2017: 25,000) due to the competitive pricing which our rich data enables.

Our COR was well ahead of our long-term target of 95%. We are also pleased to have achieved strong rates of retention across our motor and home policies book. Net claims paid during the year were £10m (2017: £2m), in line with expectations. Trading EBITDA improved significantly to a profit of £1m from a loss of £1m.

On 7 September 2017, the UK Ministry of Justice announced a draft change to the law used to set the discount rate used in calculating upfront personal injury payments (Ogden discount rate reforms). The proposal could result in a rate change from the current rate of -0.75% to a rate between 0% and 1%. It will not be applied retrospectively. The proposal, which is currently in draft form, is expected to take a few months to finalise prior to enabling legislation being effective. As a result of the uncertainty, the Insurance Underwriter reserves as at 31 January 2018 have been calculated based on the current Ogden rate of -0.75%.

The underwriting business remains well capitalised under the Solvency II capital requirements which came into effect on 1 January 2016. As at 31 January 2018, the solvency coverage headroom was approximately 60%¹. As we grow the underwriter, half the required solvency capital of up to approximately £50m can be funded from the profits of the underwriter and half from internal cash allocation.

1 Unaudited at the date of these financial statements.

New segmental reporting

In line with our new strategy, we have altered our segmental reporting to align it more closely with the way the business is managed. Roadside Assistance and Driving Services are now shown together as Roadside. Insurance Services and Insurance Underwriting are now combined as Insurance.

Head office costs have been apportioned to our two new segments. Costs are directly allocated where it is possible to do this, all other costs are allocated on the basis of a pro-rata share of revenue.

In addition to these changes, the reconciliation from Trading EBITDA to operating profit before exceptional items will now include a divisional apportionment to Roadside and Insurance for share-based payments, pension service charge adjustments and amortisation and depreciation.

	2018 £m	2017 £m
TRADING REVENUE		
Roadside Assistance	747	742
Driving Services	67	67
Roadside Revenue	814	809
Insurance Services	133	131
Insurance Underwriting	12	-
Insurance Revenue	145	131
Trading Revenue	959	940

	2018 £m	2017 £m
TRADING EBITDA		
Roadside Assistance	345	365
Driving Services	22	20
Head Office costs	(47)	(48)
Roadside Trading EBITDA	320	337
Insurance Services	79	76
Insurance Underwriting	1	(1)
Head Office costs	(9)	(9)
Insurance Trading EBITDA	71	66
Trading EBITDA	391	403

	2018 £m	2017 £m
OPERATING PROFIT		
Trading EBITDA	391	403
Share-based payments	(7)	(12)
Of which:		
Roadside	(6)	(10)
Insurance	(1)	(2)
Pension service charge adjustment ¹	(10)	(8)
Of which:		
Roadside	(8)	(7)
Insurance	(2)	(1)
Amortisation and depreciation	(70)	(67)
Of which:		
Roadside	(63)	(60)
Insurance	(7)	(7)
Operating profit before exceptional items	304	316
Exceptional operating items	3	(32)
Operating profit	307	284

¹ The pension service charge adjustment relates to the difference between the cash contributions to the pension scheme for ongoing contributions and the calculated annual service costs.

Financial review



These results demonstrate the fundamental strengths of Roadside and highlight the challenges we will address with our new strategy. Despite the delays and cost over-run of our original transformation programme, regulatory change and increased IPT, we have delivered robust results in Roadside. We are pleased with the performance of our insurance businesses.

We are confident that after resetting expectations, FY19 will be the low-point and provide a strong base from which to grow.

Martin Clarke
Chief Financial Officer



GROUP REVENUE

	2018 £m	2017 £m
Roadside	814	809
Insurance	145	131
Trading Revenue	959	940
Exceptional revenue provision	1	(7)
Group Revenue	960	933

Trading Revenue grew 2.0% to £959m, compared with £940m last year. The increase was driven principally by the strong performance of our in-house underwriter.

Roadside Trading Revenue increased by £5m to £814m. This reflected the robust performance within B2B with an increase in pay-for-use volumes as well as higher ancillary sales. This offset the decline in paid personal members as well as the anticipated reduction in Added Value Accounts (AVAs).

Roadside Trading Revenue includes the consolidated results from the 100% acquisition of AA Cars. Trading Revenue for Driving Schools and DriveTech was broadly flat.

The strong growth in Insurance Trading Revenue arose from the increased Trading Revenue for Insurance Underwriting to £12m. This growth also boosted the broker with an improvement in motor insurance policy numbers driving higher insurance broker revenue. This was slightly offset by a decline in Home Emergency Services policy volumes prior to the sale of the consumer business to HomeServe in January 2018. We will continue to report Home Emergency Services within Insurance until the migration of all of the consumer policies is complete.

Group Revenue also included a £1m release of an exceptional revenue provision relating to the £7m exceptional revenue provision for duplicate breakdown cover that we created in the prior year. In total we had provided £10m for refunds to customers of which £3m was charged to exceptional finance costs in the prior year. We agreed a programme of remediation with the regulatory authority and this programme is now substantially complete. The release of £1m reflects what we believe to be the final position for this programme. See note 21 for further information.

GROUP TRADING EBITDA

	2018 £m	2017 £m
Roadside	320	337
Insurance	71	66
Trading EBITDA	391	403
Trading EBITDA margin	40.8%	42.9%

Trading EBITDA was £391m, in line with our guidance. This 3.0% reduction from FY17 was principally due to the reduction in the Roadside Trading EBITDA. Roadside Trading EBITDA declined by £17m to £320m reflecting the higher costs from garaging due to workload peaks and the higher number of breakdowns attended. In addition, some of the growth in Trading Revenue was from lower margin activities including AA Cars, sales of parts and investment in the Connected Car proposition.

The increase in Insurance Trading EBITDA largely reflects the improved performance for both the underwriter and the broker.

Overall head office costs were broadly flat during the year with increases in IT software costs offset by continued focus on cost efficiencies. These costs have been directly allocated where it is possible to do this, all other costs are allocated on the basis of a pro-rata share of revenue: £47m (2017: £48m) to Roadside and £9m (2017: £9m) to Insurance.

Trading EBITDA margin reduced from 42.9% to 40.8% as a result of the lower profitability in the Roadside business as described above.

Financial review

continued

OPERATING PROFIT

Operating profit before exceptional items

	2018			2017		
	Roadside £m	Insurance £m	Group £m	Roadside £m	Insurance £m	Group £m
Trading EBITDA	320	71	391	337	66	403
Share-based payments	(6)	(1)	(7)	(10)	(2)	(12)
Pension service charge adjustment	(8)	(2)	(10)	(7)	(1)	(8)
Amortisation and depreciation	(63)	(7)	(70)	(60)	(7)	(67)
Operating profit before exceptional items	243	61	304	260	56	316
Exceptional operating items			3			(32)
Operating profit			307			284

Operating profit before exceptional items decreased by £12m to £304m, a year-on-year decrease of 3.8%. This reduction was largely driven by the £17m decline in Roadside Trading EBITDA and the increase in amortisation and depreciation reflecting the recent investment in transformation capital expenditure. Share-based payments in Roadside reduced, reflecting the expiration of the first vesting period for the MVP A shares (see note 34). The pension service charge adjustment increased only slightly as a result of the changes agreed with the pension trustees. Both share-based payments and the pension service charge adjustment have been allocated to segments, whereas previously they were not.

The increase in Insurance operating profit before exceptional items reflects the increase in Insurance Trading EBITDA.

Overall depreciation and amortisation for the Group increased by £3m, reflecting the progress that we have made to date on the transformation programme.

Overall exceptional items reduced from a cost of £32m to £3m income. The largest impact arose from the restructuring of the UK pension scheme which resulted in a one-off past service credit of £34m. Of this, £12m arises from the closure of the Final Salary sections of the AA UK scheme and £22m from the change in inflation indexation from RPI to CPI for the CARE (career average salary) scheme. Pensions are discussed in more detail on page 31.

Impairment of goodwill of £27m includes £26m of goodwill dating back to 2004 that had been historically allocated to Driving Schools.

Other exceptional operating items include £24m relating to business transformation (2017: £14m) offset by a £6m gain on the disposal of the home services consumer business, a £7m credit related to the reversal of share-based payment charges relating to the former Executive Chairman and a £9m improvement in onerous property provisions. The previous year's charge included £7m for duplicate breakdown cover. The remediation programme to resolve duplicate breakdown cover was completed in March 2018 and, following this, we have released £1m of the provision that is no longer required.

FINANCE COSTS

	2018 £m	2017 £m
Interest on external borrowings	132	147
Finance charges payable under finance leases	6	8
Total ongoing cash finance costs	138	155
Ongoing amortisation of debt issue fees	10	5
Net finance expense on defined benefit pension schemes	10	10
Total ongoing non-cash finance costs	20	15
Debt repayment premium and penalties	10	2
Transfer from cash flow hedge reserve for extinguishment of cash flow hedge	(2)	6
Debt issue fees immediately written off following repayment of borrowings	1	4
Duplicate breakdown cover – interest on refunds	-	3
Exceptional finance costs	9	15
Total finance costs	167	185

Total finance costs fell by £18m to £167m, with benefits of £15m from lower interest on external borrowings, £2m from lower finance charges payable under finance leases and a reduction in the non-cash adjustment to the cash flow hedge reserve. These were partly offset by the early repayment penalties of £10m incurred in the refinancing in July 2017 in which we repaid Class A1 notes of £175m and Class A4 notes of £55m as well as £98m (2017: £106m) of the Senior Term Facility.

Taxation

The tax charge for the year of £30m (2017: £26m) is made up of a current tax charge of £23m (2017: £20m) and a deferred tax charge of £7m (2017: £6m). The effective tax rate was 19.1% (2017: 22.0%). Because the Group is almost entirely UK based, we do not expect to be materially affected by the new legislation restricting the deductibility of interest by reference to UK EBITDA.

Profit and earnings per share

Profit after tax from continuing operations increased to £111m (2017: £74m) principally due to the one-off pension past service credit and the decrease in finance costs which offset the lower trading performance and impairment of goodwill. As a result, basic earnings per share from continuing operations rose by 6.0p, from 12.2p to 18.2p.

Adjusted underlying profit after tax and adjusted basic and diluted earnings per share were broadly flat at £133m (2017: £130m) and 21.8p (2017: 21.3p) respectively. The adjustments included exceptional operating items of £3m; pension service charge adjustment of £10m and penalties on early repayment of debt of £10m.

The prior year profit after tax from discontinued operations related to the sale of the Irish business and was £80m, which included £7m operating profit, a tax charge of £4m and £77m from the profit on disposal.

CASH FLOW AND LIQUIDITY

Free cash flow

	2018 £m	2017 £m
Trading EBITDA	391	403
Working capital excluding provisions and pensions	(11)	(22)
Pension deficit reduction contributions	(21)	(20)
Other items	9	10
Cash flow from continuing operating activities before exceptional items and taxation	368	371
Exceptional items and tax paid	(52)	(36)
Capital expenditure, capital payments on finance leases less proceeds from sale of fixed assets (Capex)	(86)	(96)
Interest on borrowings and finance leases less interest receivable	(140)	(149)
Acquisitions and disposals	1	99
Debt refinancing activities	(96)	(102)
Free cash flow before equity	(5)	87
Dividends paid	(56)	(55)
Net cash flows from operating activities – discontinued operations	–	10
Net increase in cash and cash equivalents	(61)	42
Cash conversion (%)	94	92

Cash conversion remained healthy at 94% (2017: 92%) and was higher than the prior year due to the reduced impact of working capital. Cash flow from continuing operating activities before exceptional items and taxation was in line with the prior year with the decline in Trading EBITDA and movement on working capital offset by a reduction in the adjustments included within other items. Excluding pensions and provisions, the change in working capital reduced by £11m compared to the prior year. Pension deficit reduction payments of £21m (2017: £20m) increased in line with the agreement in June 2017.

Capex included £34m of IT transformation capex, the final tranche of the investment originally set out at the IPO and £53m of maintenance capex offset by a £1m capex accrual. The IT investments to date have significantly strengthened and modernised the AA's foundations, particularly in the development of our dispatch system, the AA app and new digital sales platform and in the specification and development of our membership system which is yet to be fully implemented. We have also laid the foundations for growth in our Insurance business through investment in new technology and the creation of our in-house underwriter. However, more needs to be done to achieve sustainable long term growth in both Roadside and Insurance. Our strategy involves an additional £73m of growth capex over the next three years and projected maintenance capex of approximately £55m per annum.

Free cash flow before equity for continuing operations was an outflow of £5m (2017: inflow of £87m).

The Group's cash balance has decreased to £150m (2017: £211m). The debt refinancing in July 2017 led to a net cash outflow for the year of £61m (2017: £42m inflow). A new Working Capital Facility of £75m, reduced from the previous £150m facility, was put in place to 31 July 2021 on a reduced margin and currently remains undrawn. Cash is held in AAA money market funds for easy access and high liquidity.

We are required to hold segregated funds as "restricted cash" in order to satisfy regulatory requirements governing our regulated businesses, including the Insurance Underwriting business. These restricted cash balances have increased to £29m (2017: £23m) principally due to the growth in the Underwriting business.

Capital management

The Group capital is a combination of net debt and equity. As at 31 January 2018, net debt was £2.7bn while the equity market capitalisation was £0.8bn.

The Directors seek to achieve an appropriate balance between the higher return that is possible with borrowings and the advantages and security of equity funding. We aim to reduce both the amount of net debt and the cost of servicing it over time with the overall aim of lowering net debt to EBITDA to between 3 to 4 times in the medium to long term. The inevitable consequence of declining profitability in FY19 is that our leverage ratio will increase further in the next 12 months and we expect net debt to EBITDA to peak at around 7.8x in January 2019. While this level of gearing is high we intend to reduce it by growing EBITDA and generating cash to pay down debt.

In July 2017, we completed a further refinancing package which resulted in the extension of the maturity of debt and further savings in annual interest costs. We used some of our free cash flow partially to pay down debt.

The Group issued Class A6 notes for a principal amount of £250m under the multi-currency note programme listed on the Irish Stock Exchange and used the proceeds to redeem the remaining Class A1 and Class A4 notes. At the same time, the Group used available cash resources to reduce by £98m its senior term debt and extended that facility through the replacement of the existing Senior Term Facility with a new Senior Term Facility. The new facility extends the maturity of the senior term debt from 31 January 2019 to 31 July 2021.

The Class A6 notes were issued on 13 July 2017 and have an expected maturity date of 31 July 2023. The notes have a coupon of 2.75% payable semi-annually in arrears. The proceeds from the issue were used to redeem all of the remaining £175m 4.72% Class A1 notes and £55m 3.78% Class A4 notes plus make-whole payments that were paid on 31 July 2017.

As described above, a new Working Capital Facility of £75m, reduced from the previous £150m facility, was put in place to 31 July 2021 on a reduced margin. This remains undrawn.

The extension in maturity of debt means that the next repayment of borrowings is due in July 2020. The initial annual interest saving is expected to be c£3m for the years ending 31 July 2018 and 31 July 2019, then will increase to an annual interest saving of c£14m for the year ending 31 January 2020 as a result of the expiry of the existing hedging arrangements allowing the use of more of our free cash flow to pay down debt. In addition, there will be a saving of fees amounting to £0.6m following the reduction of the Working Capital Facility.

The refinancing is in line with our capital management strategy to reduce overall group borrowings as well as the associated interest cost. Since the IPO in June 2014 we have reduced gross borrowings by £623m and the annual debt interest cost on our borrowing by £90m excluding the hedging costs.

Financial review

continued

The capital structure at 31 January 2018 is summarised below:

CAPITAL STRUCTURE

	Expected maturity date	Interest rate %	Principal £m
Senior Term Facility	31 July 2021	5.71	250
Class A2 notes	31 July 2025	6.27	500
Class A3 notes	31 July 2020	4.25	500
Class A5 notes	31 January 2022	2.88	700
Class A6 notes	31 July 2023	2.75	250
Class B2 notes	31 July 2022	5.50	570
Total borrowings		4.52	2,770
Finance lease obligations			64
Cash and cash equivalents			(150)
Total net debt			2,684
Equity (valued at close on 31 January 2018)			770
Total capital			3,454

The weighted average interest rate for all borrowings of 4.52% has been calculated using the effective interest rate and carrying values on 31 January 2018.

The Company continues to evaluate the optimal refinancing strategy of its debt maturities and coupon payments including the A notes, B notes and Senior Term Facility. Early redemption of the A notes will result in make-whole interest penalties up to the date of maturity, the B2 note also has make-whole interest penalty provisions up to 31 July 2018, after which, a reducing sliding scale premium on redemption of the principal needs to be paid up to 31 July 2020. The cash generative nature of the business and the strategic priorities outlined for growth mean that we remain confident in our ability to service the interest obligations on our debt for the foreseeable future.

On 13 April 2018, S&P Global Ratings reaffirmed the credit rating of our Class A notes at BBB- and the Class B2 notes at B+.

NET DEBT

	2018 £m	2017 £m
Year ended 31 January		
Senior Term Facility	250	348
Class A notes	1,950	1,930
Less: AA Intermediate Co Limited group cash and cash equivalents	(50)	(136)
Net Senior Secured Debt ¹	2,150	2,142
Class B2 notes	570	570
Finance lease obligations	64	67
Net WBS debt ²	2,784	2,779
Less: AA plc cash and cash equivalents ³	(100)	(75)
Total net debt	2,684	2,704
AA plc Trading EBITDA	391	403
AA Intermediate Trading EBITDA ⁴	393	414
Net debt ratio ⁵	6.9x	6.7x
WBS leverage ratio ⁶	7.1x	6.7x
Senior leverage ratio ⁷	5.47x	5.2x
Class A free cash flow: debt service ⁸	3.3x	3.3x
Class B free cash flow: debt service ⁹	2.4x	2.3x

- 1 Principal amounts of the Senior Term Facility and Class A notes less AA Intermediate Co Limited group cash and cash equivalents.
- 2 WBS debt represents the borrowings and cash balances within the WBS structure headed by AA Intermediate Co Limited. This includes the principal amounts of the Senior Term Facility, Class A notes, Class B notes and finance leases less AA Intermediate Co Limited group cash and cash equivalents.
- 3 Total cash and cash equivalents for the Group excluding the value reported as the AA Intermediate Co Limited group cash and cash equivalents.
- 4 AA Intermediate Co Limited group Trading EBITDA including discontinued operations as calculated by the debt documents.
- 5 Ratio of Total Net Debt to AA plc Trading EBITDA for the last 12 months.
- 6 Ratio of Net WBS debt² to AA Intermediate Trading EBITDA for the last 12 months.
- 7 Ratio of Net Senior Secured Debt¹ to AA Intermediate Trading EBITDA for the last 12 months.
- 8 Ratio of last 12 months free cash flow to proforma debt service relating to the Senior Term Facility and Class A notes as calculated by the debt documents.
- 9 Ratio of last 12 months free cash flow to proforma debt service.

In order to comply with the requirements of the Class A notes, we are required to maintain the Class A free cash flow to debt service ratio in excess of 1.35x. The Class B2 notes require us to maintain the Class B2 free cash flow to debt service ratio in excess of 1x.

The Class A and Class B2 notes therefore place restrictions on the Group's ability to upstream cash from the key trading companies to pay external dividends and undertake those finance activities which are not restricted.

The Class A notes only permit the release of cash providing the senior leverage ratio after payment is less than 5.5x and providing there is sufficient excess cash flow to cover the payment.

The Class B2 note restrictions generally only permit the release of cash providing the fixed charge cover ratio after payment is more than 2:1 and providing that the aggregate payments do not exceed 50% of the accumulated consolidated net income.

KEY CASH RELEASE METRICS

	2018	2017
Net senior leverage (AA Intermediate Co Limited group) ¹	5.47x	5.2x
Excess cash flow ²	£91m	£194m
Fixed charge cover ratio ³	3.0x	3.0x
Consolidated net income ⁴	£208m	£214m

Note that the above table relates to the financial activities of the AA Intermediate Co Limited group and therefore will differ from those of the AA plc Group.

- 1 Ratio of net Senior Secured Debt to Trading EBITDA of AA Intermediate Co Limited group for the last 12 months. This excludes AA plc cash and cash equivalents.
- 2 Cumulative free cash flow, since 1 February 2013, reduced by dividends paid by the AA Intermediate Co Limited group and adjusted for items required by the financing documents.
- 3 Ratio of fixed finance charges to Trading EBITDA.
- 4 Cumulative profit after tax, since 1 May 2013, adjusted for items required by the financing documents and reduced by dividends paid by the AA Intermediate Co Limited group.

Dividends

We reviewed our dividend policy as part of our strategy refresh and have set a new policy. This has also had an impact on dividends for the 2018 financial year.

We recommend a final dividend of 1.4p per share in respect of FY18 subject to approval by shareholders at the forthcoming AGM. At the interim results for FY18, the Board declared that the interim dividend would be maintained at 3.6 pence per share and it was paid on 10 November 2017. Total dividends for FY18 are therefore expected to be 5p per share.

Dividend policy and proposal for FY19

The Board has changed its policy on dividends as a result of the investment outlined as part of our strategy update, and the operation of the dividend gating covenant under the Whole Business Securitisation debt structure (WBS). The release of cash from the WBS to the PLC level can only be permitted providing the senior leverage ratio (the A notes and Senior Term Facility), after payment, is less than 5.5x and providing there is sufficient excess cash flow to cover the payment. We currently have available cash of £79m at PLC level, outside of the WBS.

We propose paying two pence per share per annum from FY19 until such time as the Board is satisfied that profit and free cash flow enable a change in dividend policy.

We currently expect the dividend in respect of FY19 to be split 0.6p per share for the interim and 1.4p per share for the final.

Pensions

On 8 June 2017, the AA announced that the triennial review of the AA's UK defined benefit pension scheme had been concluded and the Trustee and the AA had come to agreement on the deficit funding plan. This plan was based on the triennial valuation of the UK's pension scheme deficit as at 31 March 2016 of £366m and compared with the previous 2013 triennial deficit valuation of £202m. The increase in the deficit was largely caused by the reduction in long-term gilt yields.

We have agreed a nine-year deficit recovery additional funding plan with the Trustee, taking into account the continued funding of the previous deficit. We will make additional contributions of:

➤ £8m per annum until March 2019

➤ £11m from April 2019 for one year

➤ £11m plus inflation per annum from April 2020

➤ £13m from April 2021 for one year

➤ £13m plus inflation per annum from April 2022 to June 2026

These will be incremental to the existing deficit reduction contributions to the UK pension scheme of £13m increasing with inflation through to 2038. The total deficit reduction payment to the UK pension scheme in the 2018 financial year was £19m. The next triennial actuarial review is scheduled as at 31 March 2019.

The UK pension deficit under the defined benefit scheme was £188m (2017: £325m), as reported under IAS 19.

The AA has also put into action the changes to the defined benefit pension scheme which has Final Salary sections and a CARE (career average revalued earnings) section. All employees that were in the Final Salary section of the scheme were moved to the existing CARE section to build up future defined pension benefits. Changes were also made to the CARE section with the inflation measure for pension indexation moved to CPI from RPI and additional employee contributions of 1.5% of salary and a change to accrual rates.

This approach has mitigated some of the recent increases in ongoing pension service costs. Overall, the changes have reduced our exposure to pension risks, increased our competitiveness within our industry and provided for a more consistent pension offering across our existing defined benefit scheme members.

Viability statement

The Board has assessed the prospects of the Company in the context of the current financial position of the Group and the principal risks described on pages 34 to 37. This assessment was considered in the context of the Group's strategic planning over a period of three years from February 2018. The Directors considered a number of potential downside scenarios to the Group's plan. These related to the Principal Risks on a scale of the potential impact based on the probability of occurrence.

The ability of the Group to refinance its debt on the various expected maturity dates (as disclosed in note 20) is a key assumption within this assessment. Following the refinancing in both December 2016 and July 2017, the Group has significantly reduced the amount of borrowings due with the next three years, however the Group will have to refinance £500m A3 notes (due 31 July 2020) over this period. The Directors continue to believe that, given the high liquidity of the sterling bond markets, the recent strong take-up of the new Class A5 note issue in December 2016 and the A6 note issued in July 2017, and the strong cash flows of the business, the likelihood of an inability to refinance is very low. In addition, the Directors would expect to refinance these borrowings in advance of the due date so that the Group continues to have access to a number of refinancing opportunities including bond issues, bank borrowings and repayment from existing cash resources. If the Class A notes or the Senior Term Facility are not repaid within 12 months of their due date, then the WBS group will be restricted in its ability to pay dividends until those borrowings are refinanced.

The Class A notes are currently rated as BBB- and this was reaffirmed by S&P Global Ratings on 13 April 2018. In the event of a downgrade, there is no immediate operational or financial impact on the business. In the event that the rating is not reinstated by the time of a refinancing of the Class A notes, there would be no restriction on the Group's ability to refinance although this is likely to be at a higher coupon value. In the event that the rating is not reinstated by the time of a refinancing of a Class B2 note, the Group will be unable to refinance these notes within the WBS and will have to find an alternative source of funding.

As a highly leveraged business, the Group is subject to loan covenants as well as the requirement to pay liabilities when they fall due. The plan and downside scenarios were therefore assessed in this context and the business remained comfortably able to make payments and comply with covenants over the forecast period.

Finally the Board considered what level of stress would cause the business viability to be put into question by means of a reverse stress test. This indicated that the viability of the business would be threatened by an unexpected cash outflow of £105m in each year of the current 3 year strategic planning horizon. Any usage of free cash flow on deleveraging over this 3 year period will reduce this headroom. The Directors felt it unlikely that an unexpected outflow of this magnitude would occur.

Having considered all these elements of the assessment carefully, the Board has a reasonable expectation that the business will continue in operation and meet its liabilities as they fall due for at least as long as the strategic planning time horizon.



Martin Clarke
Chief Financial Officer

Risk Management

Effective risk management is key to the delivery of the AA strategic objectives.

AA Risk Management Framework

Risk Registers

Our Risk Management Framework Policy requires all areas of the business to maintain a risk register which is to be reviewed on a regular basis. Risks from this “bottom up” risk identification exercise are linked to the principal risks identified by the AA plc Board which are documented in this Annual Report & Accounts on pages 34 to 37. Each risk register ‘owner’ is required to formally self-certify the completeness and correctness of their risk register(s) on a quarterly basis and confirm the effectiveness of the corresponding controls. This helps underpin the Risk Management Framework. In addition, each senior member of the Management team has his/her own set of “Top Risks” which are reviewed regularly.

Risk assessment

Risks are assessed and scored for probability and impact, both inherently (i.e. without controls) and residually (i.e. with controls). A target risk score is also set. If the residual risk score is higher than the target score, then appropriate action is agreed to ensure the risk exposure is at the desired target level.

Incidents and near misses

An important part of the Risk Management Framework is the identification and reporting of incidents and near misses including root cause analysis. This helps inform the assessment of risk and highlights areas for control improvement actions. The AA encourages and fosters a culture of open and honest incident and near miss reporting.

Key risk indicators/tolerances

The Risk Management Framework is also supported by key risk indicator management information. This is used to monitor the position against the desired risk exposure and to monitor trends and changing factors enabling early corrective action. Where applicable, tolerance levels have been set for risks. Management information reporting provides regular updates to ensure that the risk exposure remains within the desired tolerance level, or is brought to the attention of the relevant management for corrective actions to be agreed and monitored to completion.

Control verification

The effectiveness of primary controls for key risks are verified by the operation and reporting of management “snap checks” (control effectiveness tests).

Remedial actions

Management actions are documented, implemented and reported to the appropriate risk forum and tracked to resolution, if any of the following issues arise:

- > Risk exposure greater than desired target
- > A significant incident or near miss occurs that indicates a control deficiency or previously undocumented risk exposure
- > Adverse key risk indicator/tolerance reporting
- > Adverse ‘snap check’ results
- > Issues arising from audit, compliance and other reviews

Principal risks

The Directors regularly review the principal risks facing the Group, including those that would threaten business strategy. These risks are detailed below together with the key mitigating actions/controls, a summary of changes during the year and the primary key performance indicators (KPIs).

Risk appetite

The risk appetite for the AA is documented and approved by the Risk Committee on behalf of the Board. The AA’s Risk Appetite Framework defines the amount of risk the organisation is willing to take in achieving its strategic objectives.

The AA brand and the positive perception and promotion of the AA brand are key to the continuing success of the AA. The Group therefore seeks to mitigate, control or avoid risks which may have a negative impact on the brand.

Many of the AA’s activities relate to successfully managing logistics – roadside repair and recovery, arranging suitable insurance and financial products. Our customers trust us to source/provide products and services which deliver good customer outcomes.

The AA relies on a number of business partners and believes they should be fairly treated and that the AA should ensure that these partners provide services and products of a suitable standard to both the AA and AA members.

With our heritage as a membership organisation, we have a strong sense of customer fairness and therefore seek to avoid potential conduct risk, unethical behaviours and unfair customer outcomes.

The AA will accept a considered and balanced exposure to risks in order to acquire, grow or defend market share.

The AA has a zero appetite for systemic non-compliance with legal and regulatory requirements.

We are exposed to movements in the market value of assets (particularly asset values in the Pension Fund) and interest rates on a proportion of our debt. We do not take market risks for reward and use appropriate risk management techniques to reduce the effects of market risk on the Group including interest rate hedging.

The AA seeks to obtain the best available return on its cash commensurate with its risk appetite, minimising credit risk exposure to any one particular institution and maintaining a balanced investment portfolio.

The AA seeks to ensure that sufficient liquidity is always available to meet the immediate requirements of the Group.

Appropriate and effective business risk reporting has been put in place to track the position against risk appetite. These reporting arrangements are regularly reviewed for adequacy and effectiveness.

Three lines of defence

The Company operates a “three lines of defence” model. The model distinguishes between functions that have prime responsibility for identifying, owning and managing risks (first line), oversight and control functions (second line) and functions providing independent assurance (third line). All three lines of defence have specific tasks in the internal control governance framework. In the light of the increase in regulation and continued focus on governance, risk management and compliance, the Company has recently recruited an experienced Chief Risk Officer to strengthen its second line capability.

Control assurance map

Our control assurance map takes information from the risk and control output of the first line of defence to highlight the most significant risks and to indicate any areas where controls are not operating effectively or there have been risk incidents. The map also contains the principal risks identified by the Board. Onto this we map the second line – Compliance and Risk Monitoring – and third line – Internal Audit – assurance activity for the current year, prior year and year ahead to provide a view on the coverage of these assignments as well as the ratings of those assignments that have been completed. This is designed to help ensure the assurance plans cover the most appropriate areas.

Risk Model

The AA uses a bullseye risk model to guide the business in the identification of risks to the organisation. This considers core (including evolving), transitional, strategic and horizon/emerging risks.

> Core risks

The risks that are a daily part of our business activities (business as usual risks). They may be constant or may be evolving over time.

> Transitional risks

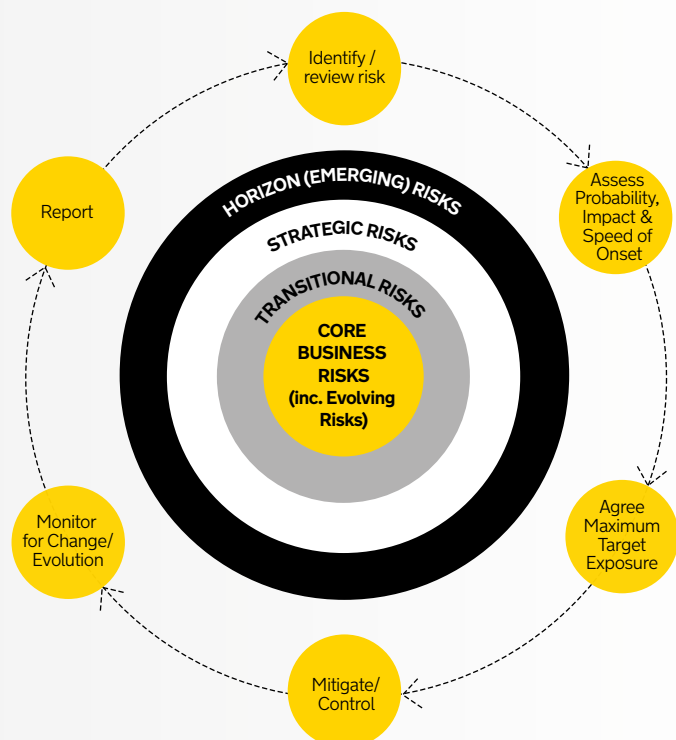
The risks that are present as a result of initiating and making changes.

> Strategic risks

Any risk that may adversely impact upon the delivery of a strategic objective.

> ‘Horizon’ (or emerging) risks

New/potential threats or opportunities that we need to prepare for. These are also considered as part of the strategy and three-year planning process.



Risk Management

continued

Principal risks

Innovate and grow Roadside



1. Outstanding service

We are unable to maintain an outstanding service

Risk trend ↗

Primary KPIs (see pages 22 and 23)

› Breakdowns attended

Description

The AA's brand and its continued success, and, in particular, the loyalty of its customers, relies on delivering outstanding service that is superior to the rest of the market. Inadequate investment in technology, systems, people and processes would place this objective at increasing risk.

Mitigation

We will continue to protect the ability of our Patrols to provide excellent service through providing them with connectivity to state of the art scheduling systems, investing in in-van technology and equipment and providing excellent training and support.

Ongoing monitoring of complaints, press reports and social media through structured processes,

including Compliance and Risk oversight, helps inform our service performance and offerings.

Change in the year

While our repair rate and single-task completion are at an 11-year high and under-bonnet times a 9-year low, restricted operational flexibility and extreme weather events resulted in an increased use of third party garages in busy periods which added cost and decreased profitability. Work is ongoing to increase the flexibility of the patrol force, reduce cost and improve customer service. Our AA breakdown app has now been downloaded by more than one million personal members and is being actively used in 29% of breakdowns.

Also see pages 24 and 25 for further details on Our performance during the year.

Impact, likelihood and trend

Delivering outstanding service is fundamental to our future and our brand. The impact of failure to deliver the best service in the market would be very high. The actions we are taking to increase the flexibility of the patrol force and improve our forecasting will reduce the probability of this risk crystallising.

Inclement weather will always have an impact on demand and we are revisiting our winter surge plan to make sure we are in the best position to deal with significant weather extremes.

2. Roadside market share and margin

We are unable to maintain our market share and an ability to command a price premium on our roadside services

Risk trend ↔

Primary KPIs (see pages 22 and 23)

› Paid personal members

› Business customers

› Average income per member

› Average income per business customer

Description

Competitors, such as Green Flag, that provide roadside services at a lower price or have a different business model together with changes in car technology threaten our market share. If we charge a price premium that is above what our service can sustain, we will not grow our member or B2B customer base and, in the long-term, sustainably grow profits. We need to improve, innovate, demonstrate and deliver a superior proposition and ensure our pricing is competitive relative to this position.

Mitigation

We are continuing to improve our roadside membership proposition by strengthening our roadside product offerings and engaging more members in additional benefits.

We have put in place processes for significantly more effective advertising campaigns and are introducing new CRM systems to improve our communications with members, which includes engaging members in their existing services and benefits to drive loyalty.

Our pricing team has significant expertise to monitor market pricing levels.

Change in the year

Car Genie, our Connected Car product, was launched during the year.

Also see "Market context" for further details on our position in the market including threats from improving car reliability, electric vehicles, car pooling, Connected Car and autonomous vehicles and how, if we react appropriately, these can be opportunities for the AA.

Also see "Our business model" for details on the competitive landscape.

Impact, likelihood and trend

Long-term the AA will find it challenging to grow profit sustainably if its membership is declining. Therefore, the impact of membership growth is critical in the long-term, as is maintaining key business relationships such as the Lloyds Banking Group contract which is up for renewal in 2018.

Membership has remained relatively stable in the last 12 months.

The business is focused on realising a sustainably growing membership and recognises the need for a more distinctive and differentiated offering to mitigate competitive pressures.

Principal risks

Accelerate growth in Insurance



3. Insurance broking business

Price comparison sites will further damage the insurance broker model

Risk trend ↘

Primary KPIs (see pages 22 and 23)

› Insurance policies

› Average income per motor and home policy

Description

The consumer use of price comparison sites may continue to transfer value from our insurance broking business.

Mitigation

We continue to use our strengths in the brand, channels and data to mitigate this risk.

Change in the year

Our Motor Insurance book has increased in the year as a result of the growth in our underwriter and roll out of insurer hosted pricing. The Home Insurance book declined as we took a longer term approach to our underwriting strategy and product offerings.




Also see "Market context" for further details on our position in the market including threats from claims and premium inflation, developing scale, technology and regulation and legislation and how, if we react appropriately, these can be opportunities for the AA.





Also see "Our business model" for details on the competitive landscape.

Impact, likelihood and trend

The competitive threat from aggregators remains unchanged, however the success of our in-house underwriter and the adoption of insurer hosted pricing enables us to better respond to this threat. We will broaden our footprint by targeting new customers who have never been members of the AA, and younger drivers.

Key: Impact, likelihood and trend

 Decrease in risk profile
  Same as last year
  Increase in risk profile
  New risk

Principal risks	Accelerate growth in Insurance (continued)		
4. Insurance underwriting Higher than anticipated claims costs Risk trend  Primary KPI (see pages 22 and 23) > Underwritten insurance policies	Description There are risks of higher than expected claims frequency, higher average cost per claim or catastrophic claims. Mitigation Strict underwriting guidelines are used to reduce claims frequency, development and costs. The reinsurance structure using co-insurance and quota share proportionately reduces the AA's	risk. Excess of loss reinsurance is also used to protect against costly individual claims. Change in the year Our in house underwriter, launched in January 2016, (a member of our Broking panel) continues to grow its Motor and Home books. Also see "Our business model" on pages 5-7 for details on the competitive landscape.	Impact, likelihood and trend The occurrence of very large one-off claims is expected to be low in volume but we have reinsurance arrangements in place which caps our maximum exposure per claim. The occurrence of smaller claims is built into our pricing models and is carefully monitored.
Principal risks	Operational and Service Excellence		
5. Business transformation We are unable to successfully complete essential business transformation Risk trend 	Description We must continue to transform the AA to achieve the required efficient customer centric services and to develop the business. There is still much to do and the required improvements to process, embedded ways of working and culture, inherently involves risks in a customer facing service environment. Mitigation There is an ongoing cost efficiency and process improvement	programme in place with progress tracked at regular Management Business Reviews. A rigorous approach is taken in implementing changes to achieve satisfactory control, with ongoing monitoring and reporting. We have a talent management model in place, where skills gaps are identified and development and/or recruitment initiatives are actioned. Change in the year The year has seen increasing management and employee stretch as the various change and product	development initiatives have been rolled out. The AA has invested in people to effectively manage transformation in the business, with the recruitment of a new COO, CIO and a dedicated transformation team. Also see "Our strategy" on page 14 for further details on transformation. Impact, likelihood and trend Strong management capability and oversight have been put in place to better manage this risk.
6. IT transformation We are unable to successfully deliver the essential IT transformation required Risk trend 	Description An essential programme of renewal and enhancement of our IT estates is in progress to address the risks to our brand and our competitive capability. The IT transformation is extensive and involves a continuing complex programme of work. Given the scale and complexity, the programme involves inherent risks to the timely delivery of this implementation. Mitigation Proven methodology with specialist IT development skills is in place to manage this risk. The programme is being led by executives with a proven track record in IT transformation.	The programme is subject to considerable scrutiny by the executive management team and regular progress reports are reviewed by both the Risk Committee and the Board. Change in the year Investment in new IT systems over the last three years has improved our productivity and marketing and digital capabilities. We have committed to slowing the pace of the implementation phase to mitigate the risk of management stretch and ensure adequate impact assessments are undertaken. We are building on the strong, new foundations now in place.	Further investment in IT development forms part of the new strategy. Also see "Our strategy" on page 14 for further details on transformation. Impact, likelihood and trend The ability to manage and enhance existing legacy systems as well as implementing new IT systems are key to the successful ongoing development of the AA. The adverse impact of a material delay to the implementation of the programme would be high.
7. Safety We are unable to maintain the safety of our workforce and members Risk trend  New	Description We must continue to effectively manage the risks to the safety of our workforce and members and ensure controls are deployed to achieve this. Accountability to take action is essential in this as oversight, review and embracing continual improvement. Mitigation We have a robust and externally audited integrated health, safety and environmental (HS&E) management system as well as local arrangements where appropriate. We regularly review all our HS&E risks and controls to ensure they remain fit for purpose. We have in place safety improvement programmes which are SMART and drive the continual improvements we aspire to.	We have a robust monitoring and assurance process which includes safety performance and is reviewed at the PLC Risk Committee and the Executive Risk and Compliance Committee. We have a dedicated team of health and safety advisors who are all members of the chartered body IOSH (Institution of Occupational Safety and Health). Change in the year This is a new principal risk. The AA continues to strive to maintain a safe environment for employees and members. Please also refer to the Corporate Responsibility section on page 42 for detailed performance this year. Impact, likelihood and trend Protecting our employees' safety whilst they are at work is fundamental to our values and our brand.	The impact of failure to look after our employees would be very high and could result in not only death or serious injury, but an increase in civil claims and enforcement action against the Company and/or its Directors. Protecting our members is also of paramount importance. As the market leader for roadside repair and recovery our members' safety is always considered when agreeing working practices. This will always be the case and members can rely on the AA to put safety first. The consequences of poor safety at the roadside can be fatal. AA working practices are designed to reduce the probability of accidents to a minimum although given the environment in which we provide roadside service it is not possible to eliminate this risk.

Risk Management

continued

Principal risks

Create a High Performance Culture



8. Growing the business

We are unable to grow the business in a manner that complements and sustains the brand

Risk trend

Primary KPIs (see pages 22 and 23)

> Paid personal members

> Insurance policies

> Franchised driving instructors

> Trading EBITDA

Description

We may be unable to develop and grow new profitable business products and lines that complement the customer experience and which demonstrate standards and values that underlie our core brand.

Mitigation

We continue to pursue new opportunities that complement our core brand.

Proposed new products and changes to existing products are put through our product development process and are reviewed by the Product Outcomes Forum, (which meets frequently throughout the

year) and includes Executive and senior attendees from the various business areas together with Compliance and Risk oversight.

Change in the year

A new business strategy was announced in February 2018 to innovate and grow the Roadside business and invest to accelerate the growth of the Insurance business.

We expect increased product innovation aligned to our Connected Car and insurance growth strategy.

Also see Our performance on page 24 for comparisons with our position in the previous financial year.

Impact, likelihood and trend

The immediate impact is low as this is more a long term matter.

In the long term without our effective control framework which is in place, our products would become uncompetitive, less relevant to the market place and fail to keep pace with member and customer needs.

We are uniquely positioned to play a central role in shaping the way the market reacts to emerging trends, such as Connected Car, electric and hybrid vehicle growth and changing ownership models.

9. Our people

Ineffective human resources to achieve the AA objectives

Risk trend New

Description

Failure to recruit, train, develop and retain employees who have the skills and experience required by the business. Employee costs excessive. Staff of insufficient calibre.

Mitigation

The AA operates an emerging talent programme to help develop employees through external qualifications. To attract and develop new talent we operate apprentice schemes for both indoor and outdoor roles.

Change in the year

Our recent employment engagement survey highlighted a number of

cultural challenges and employee morale issues. A plan is in place to improve the AA as a place to work and we have established channels for open communication.

Following the dismissal of Bob Mackenzie (see page 50 for further details) our corporate governance has been significantly improved by splitting the roles of CEO and Chairman.

Simon Breakwell has initiated a number of senior management changes and a full review of our priorities to ensure we have the right resources focused on the correct activity. Significant re-organisations

have taken place in our contact centres.

Please also refer to the Corporate Responsibility section on page 40 for further details.

Impact, likelihood and trend

If the AA does not have the right people skills in sufficient numbers, this will impact on our ability to deliver our strategy and three-year plan and the level of customer service which is expected from the AA brand.

Principal risks

Financial and other



10. Debt leverage and pensions

Debt: We are unable to manage our debt

Risk trend

Primary KPIs (see pages 22 and 23)

> Leverage

> Interest cover

> Trading EBITDA

> Free cash flow before equity

Description

The Company is unable to repay or refinance its debt at an acceptable price.

Mitigation

We have strong recurring cash flows which support the current capital structure, and which will enable us to reduce leverage over time in line with our stated strategy.

Change in the year

The Company completed a further debt refinancing structuring this year taking advantage of the low interest rate environment to reduce near term debt. No debt is due to be repaid until 31 July 2020 (the A3 notes). In order for the Group to be able to refinance

its borrowings, it is a key assumption of the Directors that the Capital Markets remain open to the Group. The Directors continue to be confident that they will be able to refinance these borrowings at an acceptable price. We will continue to make additional repayments to reduce the debt burden as opportunities for this arise.

Whilst the Company remains highly leveraged, this further restructuring improves the ability of the Company to manage unforeseen financial shocks.

Please also refer to the Financial review on pages 27 to 31.

Impact, likelihood and trend

If this risk materialised, the Group's bondholders would appoint an administrative receiver to run the business for cash until all secured debt is repaid. However, the AA continues to be a high cash generating organisation and the likelihood is therefore very low. A downgrade of the Class A notes would impact our ability to refinance (see the viability statement). However, S&P have recently reaffirmed the current ratings.

Interest rates may increase in the future and may therefore be higher when debt is due to be repaid or refinanced in July 2020.

Pension: We are unable to meet our pension liabilities

Risk trend

Primary KPIs (see pages 22 and 23)

> Trading EBITDA

Description

The Company has a large defined benefit (DB) pension scheme, currently in deficit, whose assets and obligations are subject to future variation from investment returns, longevity and other similar factors.

Mitigation

The UK pension scheme is supported by a company covenant and the assets and obligations of the scheme are kept under review. The DB scheme is closed to new entrants.

Change in the year

A pension consultation process with employees has been successfully completed and changes to the pension schemes implemented, including closure of the final salary pension scheme and move of participants to the Career Average Section, to mitigate future exposure on the pension liability risk. The Group is still exposed to future variation from investment returns, longevity and other similar factors. In June 2017 the Group completed the triennial valuation of the UK




pension scheme agreeing a funding deficit of £366m. We have agreed a nine-year deficit recovery additional funding plan with the Trustee, taking into account the continued funding of the previous deficit.

See note 25 of the financial statements.

Impact, likelihood and trend

With the potential continuing volatility in the markets and global economic uncertainty the likelihood of the risk of increasing pension deficits remains high.

Key: Impact, likelihood and trend

 Decrease in risk profile
  Same as last year
  Increase in risk profile
  New risk

Principal risks**Financial and other****11. Information security/Cyber crime/Data breach**

We are unable to protect ourselves from a significant data breach or cyber security incident

Risk trend 

Description

Critical information is not available where and when it is needed. The integrity of critical information is corrupted or the confidentiality of commercially sensitive, private or customer information is compromised by inappropriate disclosure. A serious data breach occurs.

Mitigation

The AA has an ongoing programme of security improvements to maintain a suitable level of security for the increasingly sophisticated world-wide cyber threats. Controls include information security awareness training, preventative and detective security, a specialist information security team, and information security requirements being included in third party arrangements.

The AA benchmarks its security controls against the Center for Protection of National Infrastructure (CPNI) and associated Critical Security Controls (CSC).

Change in the year

While we have made further progress enhancing our IT security and defences against cyber-crime, the external environment continues to be increasingly hostile to all businesses. A third party provider of services to the AA had an incorrectly configured server and this exposed data for 91,590 customers. The vulnerability in the third party's systems was closed promptly when it was identified. An exercise was undertaken to communicate with the affected customers and the matter was reported to the ICO and the FCA, although it did not arise in

our regulated business. We consider this to be an emerging/evolving risk and will continue to take additional steps to improve our controls, taking guidance from external specialists.

We have recently hired a Data Protection Officer and a new Information Security Officer to strengthen the management of this area.

Impact, likelihood and trend

As for any company the impact of this risk crystallising could be substantial. The external environment continues to be increasingly hostile to all businesses with cyber-attacks on companies continuing to be more sophisticated and more frequent.

12. Regulatory and legal environment

A changing regulatory environment may adversely affect our activities
Material litigation against the AA

Risk trend 

Description

The changing regulatory environment could cause currently compliant services to become non-compliant, with material implications to customer offerings, pricing and profitability.

Failure to comply with regulatory obligations could result in fines and reputational damage.

Changes in Government legislation or taxation could impact the business model.

Mitigation

The AA has a zero appetite for systemic non-compliance with Legal and Regulatory requirements.

Close engagement with regulatory objectives is coupled with good governance and strong monitoring processes to ensure that we continue to focus on delivering products and services that result in good customer outcomes.

Regular dialogue is maintained with the FCA, the Gibraltar Financial Services Commission and other regulatory bodies.

Our Regulatory and Legal Change Committee tracks forthcoming changes and advises the business on changes required.

Products are reviewed regularly to reaffirm they are fit for purpose.

The AA has in house Legal and Compliance teams and also takes external legal advice.

Change in the year

Regulatory changes that have the potential to impact on this risk include implementation of the FCA's Insurance Distribution Directive and preparing for the Senior Managers and Certification Regime (SMCR) in 2018. A project is being initiated to prepare for the SMCR.

We have updated our renewal processes to comply with the new requirements on price transparency.

The new General Data Protection Regulation (GDPR) requirements come into force in May 2018. A major multi-disciplinary project has been put in place to prepare the AA for the changes to data protection that will come into effect.

Duplicate cover: The previously reported remediation exercise relating to duplicate breakdown cover has now been concluded.

The dismissal of Bob Mackenzie for gross misconduct has resulted in litigation which the AA will vigorously contest. See note 36.

Impact, likelihood and trend

As in previous years the regulatory environment is expected to continue to be dynamic with a continuing programme of regulatory initiatives. These additional requirements may drive further commoditisation into the market at the expense of superior service differentiation.

Continued increases in IPT could make insurance products including Roadside Assistance less affordable for our customers.

Involvement in litigation is time consuming and a distraction for the Board and the management team.

13. Brexit

Negative impact on the AA as a result of Brexit

Risk trend  New

Description

At this stage of Brexit negotiations, it is difficult to fully identify and assess potential risks. The following have been highlighted as of potential concern for the AA:

- › Passporting for insurers and other regulatory change
- › Impact on EU nationals in the UK and potential skill shortages
- › Increasing future costs of supplies and services received by the AA
- › UK recession as a result of Brexit reducing the demand for AA products and services

Mitigation

The AA's Brexit Committee meets to support the AA business in monitoring and understanding likely impacts of Brexit by:

- › Coordinating and evaluating information in respect of the potential impact of changes to external laws, regulations and codes that affect the AA business
- › Considering any other matters as may be referred to the Committee by the Board and other groups/ individuals within the AA Group in respect of the implications of Brexit on the business

Change in the year

This is a new risk and the uncertainty resulting from Brexit is already being reflected in various external and internal risks.

Impact, likelihood and trend

While at this stage in Brexit negotiations it is not possible to identify risks with certainty, concerns which may have a significant impact include:

- › Potential impact on non UK domiciled panel members/insurers
- › Impact on the services we provide covering European travel
- › Consequences for EU nationals working for the AA
- › Uncertainty on future cost base where goods/services are received from the EU/abroad
- › Changes to regulation
- › Potential recession and changes in consumer behavior impacting on demand for our products and services

The AA's commitment to Corporate Responsibility



Edmund King
AA President

As President, I head up the AA Charitable Trust and lead our campaigns on safety, mobility and environmental issues. But it is the ethos of our people which lies at the heart of what we do at the AA and at the heart of our commitment to corporate responsibility.

Following consultation with a wide range of stakeholders, including investors, suppliers, customers, NGOs and our people, we have changed our approach to CSR. In this year's report, we are setting out a new CSR strategy which is integrally linked to the AA's values and has a measurable delivery plan to ensure we achieve our aims. While it is early days, we are committed to making quick progress.

Over the next three years we are committed to delivering this strategy because it reinforces what makes this company great – our people, our Brand and our members. We have now included two of our top three CSR strategic priorities which we will be focusing on this year and next within our principal risks (see pages 34-37); and which are listed opposite.

In addition, we will continue our work to protect and respect data, taking into account the new legislation. We will also continue to support our local communities and make sure that our business partners and suppliers are aligned with our business ethics and commitments.

To further demonstrate commitment to integrating CSR into how we do business, throughout this section we have illustrated how the AA's CSR priorities are linked directly to our business model. Enabling CSR to support our wider business, we have identified the critical inputs and values needed to deliver our strategic objectives. We have also highlighted in this report, with the use of the relevant logos, how we are doing our part to help the UK deliver the 2030 Agenda for Sustainable Development and its Sustainable Development Goals.

Key CSR milestones in the 2018 financial year

1. Our people – attracting and retaining talent; effective employee engagement

- › We ran our first employee engagement survey, in several years, OurVoice, and 78% of our people participated in it
- › We have begun transforming our internal communications and engagement, developing an open, high-performance culture
- › We launched apprenticeship pathways in our Emerging Talent Programme, Evolve

2. Safety – of employees and our customers, members and the wider public

- › We had the lowest number of accidents and reportable incidents in five years
- › Over 70% of our people who took part in our CSR survey felt empowered to look after their safety and make changes to help improve safety at the AA
- › We worked with the FiA and other groups to run the "Don't text and Drive" bill-board campaign, fronted by Pharrell Williams, Rafael Nadal and Fernando Alonso. The AA Trust and Think! also produced a hard-hitting cinema advert

3. Environment – emissions from our operation

- › We reduced our scope 1 & 2 CO₂ emissions by 11% year-on-year
- › We reduced our water consumption by over 10% compared with last year

We also benchmarked ourselves against others in our industry through independent assessments:

- › We undertook the Dow Jones Sustainability Assessment for the first time. We are proud to be ranked second worldwide in the Diversified Consumer Services Sector and were recognised in the Sustainability Year Book 2018 as a sustainability leader in this sector
- › We remained a constituent of the FTSE4Good Index Series
- › Our provision of roadside services achieved above average scores compared to our industry sector peers in the Chartered Institute of Procurement and Supply (CIPS) Sustainability Index

The road to our new CSR strategy

Discovery phase

Stakeholder engagement undertaken, both with internal and external interested parties. A review of what we had in place to pull all our CSR related activity together

Materiality analysis

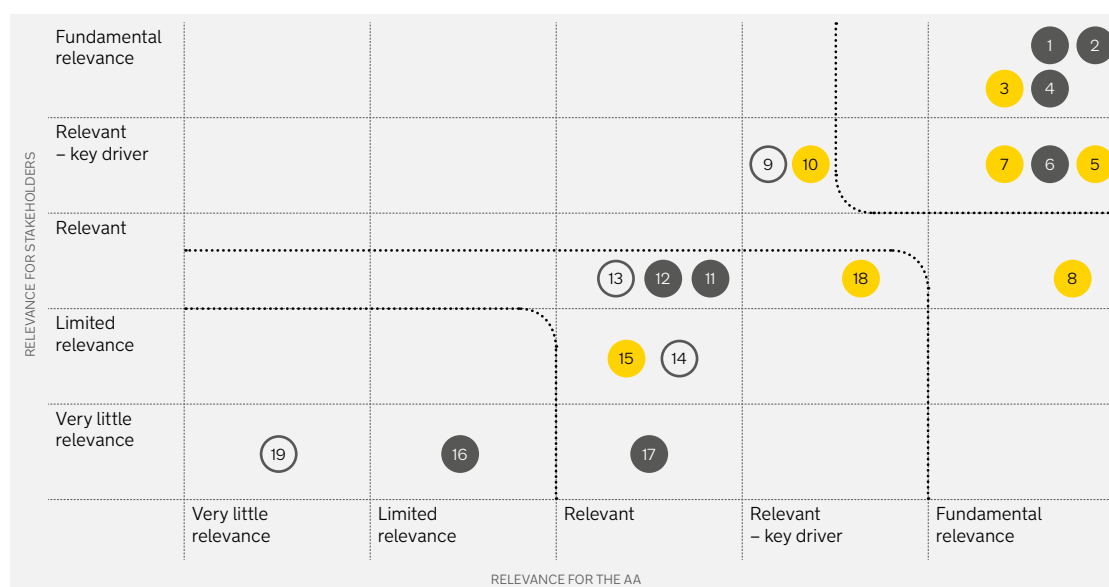
An assessment was undertaken looking at how the AA conducted its business and which aspects were of concern to our stakeholders as well as our Company, rating them for their level of importance (see materiality assessment map on p39)

Set CSR Strategy and measurable delivery plan

Our CSR Strategy – Doing the right thing because we care by:

- › Looking after our people, our members, our B2B customers, our shareholders and bondholders and the community (care)
- › Being a responsible business and the best at what we do (expertise)
- › Being a respectful and considerate business (courtesy)
- › Ensuring we are a sustainable business (dynamism)
- › Working together for a better future (collaboration)

Materiality assessment



Risk issue

● Economic

- 3 Data protection
- 5 Customer satisfaction
- 7 Responsible financial services
- 8 The future vehicle
- 10 Corporate governance
- 15 Responsible marketing
- 18 Supply chain

● Social

- 1 Safety of members/ customers
- 2 Staff health and safety
- 4 Attraction and retention of staff
- 6 Communication/ engagement
- 11 Human Rights
- 12 Diversity and equal opportunities
- 16 Local community
- 17 Campaigning and lobbying

○ Environmental

- 9 Vehicle fuel
- 13 Building energy
- 14 Waste
- 19 Water consumption

The AA's commitment to Corporate Responsibility

continued

Priority 1.

Our people

CRITICAL INPUTS

- > Financial resources
- > **People**
- > **Brand**
- > Intellectual property and data
- > Technology

VALUES

- > **Courtesy**
- > **Care**
- > **Expertise**
- > Dynamism
- > **Collaboration**

Find out more
Our business
model P5

Achieving our strategic priorities depends on our people. They represent our Company among customers and communities. Our aim is to be a great place to work, providing interesting and challenging opportunities, excellent career progression, a collaborative, inclusive and values-based culture for our people. This is the key to creating value for all our stakeholders which is why our people are identified as a principal risk to the successful and sustainable operation of our service. The most significant areas which impact this risk are:

- > Attracting the right talent/our employer brand
- > Retaining talent through development, engagement and wellbeing
- > Gender and diversity
- > Anti-corruption and anti-bribery

These areas are controlled through our policies and processes as well as the monitoring of our management and control strategies through regular reviews with senior management. Both internal and external audits are undertaken as part of the ISO certifications relating to our road operations.



Attracting talent and developing our employer brand

This year we launched the new AA careers website www.theaacareers.co.uk which won an award in the 2017 National Online Recruitment Awards (NORAs) against some stiff competition. The NORAs views the recruitment sector from the perspective of the jobseeker, shining a light on the very best examples in our industry. Organisations in our category included LV=, McLaren, British Gas, npower and The National Trust.

To deliver the required attraction levels we have adopted a combination of recruitment channels all with a new common creative theme and messaging, to underscore the new central careers site employer brand message: Ready for Anything. We also entered a partnership for candidate management to ensure we're able to deal with the volume of applications and take care of the candidate experience.

This fundamental change in recruitment strategy and brand messaging has helped attract over 30,000 candidate applications (up 200%) and recruit almost 700 new employees during 2017.

The AA currently offers Level 2/3 apprenticeship programmes within our indoor operations, with plans to introduce these schemes across the organisation in the near future.

We continued to actively support the redeployment of armed services personnel into civilian roles, promoting AA job opportunities through both the CTP and Early Re-Settlement Magazine.

Wellbeing

Providing support for employee health and wellbeing is important to our people strategy. We provide an Employee Assistance Programme which provides free confidential 24/7 support for our people both online and over the phone. Qualified counsellors support on a range of home and work issues including medical concerns.

As one of the leading causes of illness among our people, mental health is an area of growing importance to our business. Working alongside Ben, a not-for-profit organisation which partners with the automotive industry, we have delivered a comprehensive mental health awareness training programme to all line managers who work within our Customer Operation function.

Engagement with our people

This year we ran our first engagement survey for five years. It was called OurVoice to represent all our colleagues. As employee engagement is an output of working for a company, it was important that consistency of behaviour was determined as part of the survey. Therefore, we decided to use a cultural index measurement rather than a more traditional employee engagement scoring system. This gave us a better understanding of the current employee experience and a better insight into our culture. It assessed how it feels to work in the AA as well as how we work with our colleagues and our customers. We had an excellent response with 78% participation and over 6,000 comments. The four stand out areas for action were:

- > Respecting and supporting customer facing teams and providing more support for them
- > Improving cross-team working
- > Identifying ways to improve and increase opportunities for development and career progression
- > Involving employees in sharing their ideas to improve the business

The survey results have been shared Group wide with local and functional action plans currently being developed for implementation in FY19.

Throughout this year we have focused on improving Company-wide communication, setting up a Communication and Engagement function to better support our engagement strategy. It's important that our people have a voice and the opportunity to share their thoughts, feedback and suggestions for the business. Highlights from this year have included:

- > 'Ask Simon', an email channel to our CEO Simon Breakwell was established. This has enabled our people to ask questions, contribute ideas to improve the business and to raise any concerns they may have
- > Members of the Executive addressed hundreds of colleagues and managers at quarterly business update meetings
- > The senior leadership team engaged many of our contact centre Team Leaders and Roadside Area Managers at team building and strategic planning sessions

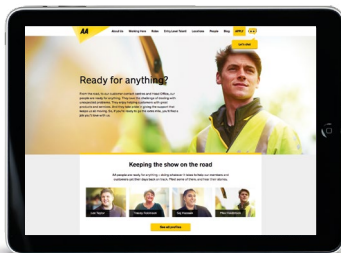
We continue to work closely with our recognised Union, the Independent Democratic Union (IDU) as well as the Management Forum (an elected group for management-level employees) to ensure our employees' views are heard, as well as meeting our legal obligation for information and consultation. Meetings dedicated to the operational area are held with the IDU once a quarter to discuss all employee-related matters, including safety and workers' rights and we engage with them on matters related to pay. It is important to us that our people are actively involved with our safety risk assessments so, wherever relevant, at least one Union representative joins the group who are carrying out the assessment to ensure they are represented.

We maintained our Employee Share Incentive Plan, giving our people an opportunity to invest in our brand and share in any success. Participants receive a free matching share for every share purchased as well as shares which represent a dividend on their holding. As at the 31 January 2018, 33% of our eligible employees participated in the plan.

We have the AA Worksave Pension Plan which offers increased employer contribution rates and life assurance cover to support our people in their retirement. In 2018, we will contact those employees auto-enrolled in line with the Government's minimum pension requirements for workers to remind them of the increase in employee and employer contributions that will occur in April 2018 as well as reminding them they are entitled to join the AA Worksave Pension Plan.



See all our award winners at theaapl.com



Developing high performance culture

This year we introduced Evolve, our Emerging Talent Programme which offers a range of development qualifications for employees at every stage in their career as well as for new Apprentices into the business. It enables us to nurture emerging talent through offering apprenticeship Pathways (industry recognised qualifications) to help our people develop their skills, knowledge and expertise while learning on-the-job, supporting their career progression. We have expert apprenticeship partners to provide support to our people every step of the way on their chosen pathway.

We rolled out the Learning Management System which we had developed in the latter part of 2016 which has enabled us to more effectively support our teams in improving their skills and continuous personal development. It provides us with a holistic view of pan-AA development with some of the highlights in its first year of release being:

- › Over 7,000 employees have completed online learning (excluding mandatory E-Learning)
- › Almost 29,000 mandatory E-Learning modules have been issued
- › New governance process implemented to ensure consistency and alignment of new training requests to employees' development plans
- › Management of all regulated training requirements ensuring our people have the right accreditation to maintain the level of service to our members and customers
- › The minimum training all staff are issued with when they join our Company, and then on a scheduled basis throughout their career are:
 - Data Protection
 - Information Security
 - Conduct Risk
 - Financial Crime Prevention
 - Complaints Handling
 - Equality and Diversity
 - Anti-Bribery
 - Treating Customers Fairly
 - Health and Safety

OUR EMPLOYEE AWARDS



The annual awards ceremony took place in London in September. All of our finalists and their partners came together for a very special AA Awards evening, where we announced 21 winners. The baton of Patrol of the Year and Recovery Patrol of the Year was passed by John Snowling and Tony Doran, to the new winners, Vince Crane and Brent Pugh, who are already passionate about the crucial roles they've been tasked with.



Gender and diversity

We are committed to supporting diversity and creating an inclusive workplace where all our people feel valued and able to fulfil their potential. We are passionate about being an equal opportunities employer and we do not discriminate on the basis of gender, religion, age, disability or ethnicity.

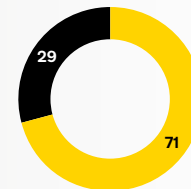
Our employment policies and practices reflect a culture where decisions are based on individual ability and potential in relation to the business needs. We are committed to ensuring that individuals are treated fairly and in a non-discriminatory way throughout the recruitment process and at all stages of their employment.

In line with the Gender Pay Gap Information Regulations which came into effect during the year the Company has published gender pay gap information on the AA website and on the Government website.

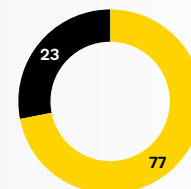
Our key controls to help us deliver an inclusive culture and diverse workforce are:

- › An Equality and Diversity policy which applies throughout the AA and is provided to all employees during their induction training
- › All our people being required to complete a mandatory Equality and Diversity module annually in order to ensure understanding and mitigate risk of non-compliance
- › Should one of our people become disabled (mentally, physically, permanently or temporarily) during employment we have processes in place so that we are able to make every effort to adjust their environment to allow them to maximise their potential and remain a valued member of the AA team
- › We monitor and seek to ensure a good balance of male and female employees throughout our Group (bearing in mind the male focus of patrols)
- › We continue to build a supportive and flexible culture that enables us to develop and retain women
- › We are members of the Disability Confident scheme
- › We have regular discussions with all disabled employees to consider changes we can make to ensure their ongoing career development

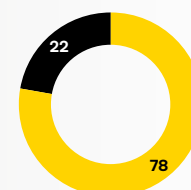
BOARD (%)



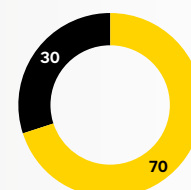
EXECUTIVE COMMITTEE (%)



LEADERSHIP TEAM (%)



ALL EMPLOYEES (%)



● Male ● Female

The AA's commitment to Corporate Responsibility continued

Priority 1.

Our people

continued

Anti-Corruption & Anti-Bribery

We are committed to undertaking our business and delivering our service with honesty and integrity. Several processes guide our approach:

- › An Anti-Bribery and Allowable Gifts, Hospitality and Donations Policy which is reviewed and re-communicated annually. Anti-bribery risk is rated and held on every appropriate departmental risk register with controls. All registers are reviewed at regular intervals. An internal audit was carried out in financial year 2017 and all actions were completed shortly afterwards including face to face training where practical
- › A Financial Crime Policy was reviewed and updated during the year. It reflects that the AA values its reputation for financial probity, professionalism and integrity and recognises that the Group has a duty to protect its customers
- › A Fraud reporting inbox is monitored by our Fraud team
- › A Whistleblowing policy encourages employees to confidently raise concerns internally so that these can be investigated in an independent, timely and effective manner. This helps us to ensure that our commitment to conducting our business with honesty and integrity is met. During the year, ten cases were escalated for review by HR and the Executive Risk and Compliance Committee, all have been investigated and concluded. Some of the consistent themes included allegations regarding staff conduct, management behaviour, discrimination and performance management
- › Secretariat holds registers of Directors' interests and external appointments, plus situational and transactional conflicts of interest and central gifts register
- › We have implemented mandatory anti-corruption and anti-bribery e-Learning training for all staff; this is distributed to staff as they join the organisation to complete, and then on a scheduled basis throughout their career

As a result of this approach we are pleased to report that we have received no enforcement action, fines, penalties or settlements in relation to corruption or bribery. Also, no member of AA staff has been identified to us as being involved in corruption or bribery while representing or undertaking the AA's work.

Priority 2.

Safety

CRITICAL INPUTS

- › Financial resources
- › People
- › Brand
- › Intellectual property and data
- › Technology

VALUES

- › Courtesy
- › Care
- › Expertise
- › Dynamism
- › Collaboration



Find out more
Our business model
P5



We are dedicated to providing a sustainable, expert and dynamic service to our customers that demonstrates we care by delivering operational excellence through high standards of health, safety and environmental (HS&E) management. In line with our policy, we aim to continually improve our HS&E performance, always seeking to reduce any risks. We believe in always doing the right thing and in doing it safely, without unnecessary risk to people's health or to the environment.

To demonstrate our commitment we continue to have our management system externally audited to the OSHAS18001 standard.

While DriveTech is the business that is in scope for certification purposes, the management system applies to all our operations; they are internally audited for the effective implementation of it. Alongside this audit programme we monitor the effectiveness of our management strategies through regular performance reviews with senior management. The Roadside operation continues to be certified to PAS43, the publicly available management system specification for the safe working of vehicle breakdown and recovery operations. We require all of our garage agents to hold this standard too.

As detailed within our principal risks (pages 34-37), safety is material to the successful operation of the AA. The most significant safety related risks our people face when delivering service to our customers and members are:

Top safety risks:

Risk	Control	Performance
Manual handling	We control this risk through regular reviews of our systems of work and equipment design and by ensuring staff carrying out this type of work are regularly trained in the techniques we use to minimise the risk of injury.	We have seen a slight increase (4%) in the accidents involving this activity compared to last year. As a result, we have improved our training and started to implement just-in-time safety instructions.
Driving for work	We minimise this risk through driver assessment and training, maintenance and servicing regimes for our vehicles, deployment, telematics and navigation systems for our patrols and by minimising in-vehicle distractions in our fleet.	Compared to last year, we have achieved a reduction of road traffic collisions of over 7%.
Lone working	To minimise the risks associated with lone working we have in place man down procedures and vehicle tracking systems. We also have support and guidance available relating to violence and abuse and how to minimise and manage this risk should it occur.	Compared to last year we have achieved a reduction of 5% in incidents involving violence and abuse.
Slip, trip, falls	We control this risk in the offices through maintenance and inspection regimes, and through training and PPE for our workforce who are delivering our service off site.	Compared to last year we have achieved a slight reduction of 2% in accidents of this type.

a. Accident performance

We continue to maintain our record of zero fatalities. The number of major injuries we report to the Health and Safety Executive (HSE) remains lower than the national rate for industries operating in a similar environment.

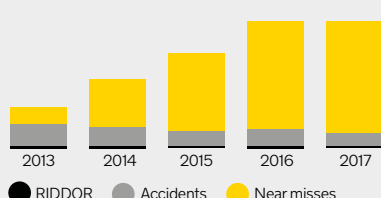
We continued to maintain our high gas safety standards with no Health and Safety Executive or Gas Safe action being taken.

Last year we reported that, following a change in our procedures to encourage a focus on safety with our patrols, we had seen an increase in accident numbers. Significant focus has been given to this area throughout this year to address the increase. Highlights this year include:

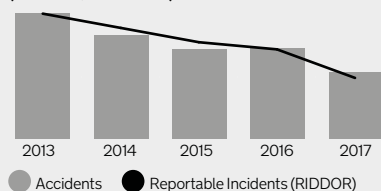
- › Behavioural safety programme trialled
- › New communication platforms utilised to deliver the safety message, including an HSE Blog for managers of our field based teams and dedicated quarterly team safety briefings for the patrol force
- › Updating and re-focusing our HSE induction training for patrols
- › Trialling new tools and equipment to further minimise safety risks

As a result of this focus and effort, we are very pleased to report that, this year, we have achieved not only the lowest number of accidents and reportable incidents (reportable under the Reporting of Diseases and Dangerous Occurrences Regulations (RIDDOR)) in the last five years, but also the lowest frequency rates for that period too. Our outstanding near miss reporting also continues to enable us to make a positive impact on risk reduction.

SAFETY INCIDENT REPORTS



INCIDENT FREQUENCY REPORT (PER 100,000 JOBS)



b. Partnerships

We have entered into a collaborative partnership with the Hampshire Fire and Rescue Service under the Primary Authority Scheme. This provides us with the facility to identify opportunities to improve our current fire risk management systems and processes as well as looking to implement any best practices.

c. Our members and customers

With the introduction of more smart motorways we have introduced a system for our breakdown emergency call handlers to immediately identify where a member has broken in an area with no hard shoulder. The call handler can quickly establish if the member is in a live lane, high-risk situation and immediately contacting the emergency services via a 3-way call facility.

d. The industry

SURVIVE work

We remain an active member of the SURVIVE Group, an industry led body that aims to make working at the roadside safer. This year we collaborated with Highways England and the Institute of Vehicle Recovery Operators to undertake a detailed review of the different breakdown scenarios that can occur on a smart motorway. As a result, a video was launched to the industry at the European Tow Show showing the best practice for breakdown management. The SURVIVE best practice guidelines (used by the industry as a safe system of work) were also updated.

Gas Safe

The AA instigated and drove forward a new Gas Safe technical bulletin covering the issue of sealing flues which was issued towards the end of 2017. We not only seek to improve safety within our workforce and for customers/members, but we are also committed to driving best practice in the industries in which we operate.

Take Care campaign

We continued to run the Take Care campaign which has, at its heart, a commitment to develop a safety culture in which empowerment and accountability are central at all levels and our people are enabled to take improvement actions. The CSR stakeholder engagement survey assessed the effectiveness of this campaign with our employees and:

Over 97% felt it was important for the AA to look after H&S

Over 77% felt that we were managing H&S to either the right level or above

Over 70% felt empowered to look after their safety and change things to help improve safety in the AA



The AA's commitment to Corporate Responsibility

continued

Priority 3.

Environment

CRITICAL INPUTS

- > Financial resources
- > People
- > **Brand**
- > Intellectual property and data
- > **Technology**

VALUES

- > **Courtesy**
- > **Care**
- > **Expertise**
- > **Dynamism**
- > Collaboration



Find out more
Our business model
P5



The assessment of our environmental risks and implementing effective management strategies to minimise their impacts are integral to our business. Our key environmental impacts are:

- > Emissions from the fuel used in our operational vehicles and company cars
- > Electricity, gas and water used in our buildings
- > Waste and its disposal

These are controlled through our policies, environmental management system processes and the implementation of measurable plans to reduce each of these impacts and drive continual improvement. We monitor the effectiveness of our management strategies through regular reviews with senior management. Both internal and external audits are undertaken as part of the ISO14001 certification relating to our road operations and the sites from which they operate.

Our ongoing programme to deliver a high-quality service to our members in a way that minimises our impact on the environment has continued with some key achievements during the year, which include the following:

Electric Vehicle Training Rig

As vehicle technologies develop, the volume of hybrid and electric vehicles is set to grow in the coming years as we move away from conventional engine technologies. To remain ahead of these changes, this year the AA technical team took delivery of the first ever Hybrid training rig based on a Toyota Prius system. Using our technical expertise, the AA team worked tirelessly with rig manufacturers (A.G. Block) to develop and produce this. Our investment will ensure our patrols remain experts in this field of vehicle technologies, capable of meeting our customers' needs at the roadside.

The car of the future and supporting the changing vehicle profile in the UK

The AA is working in partnership with Chargemaster POLAR network to allow free EV charging for customers stranded without charge. A trial was run in the South East and London towards the end of 2017, with national rollout planned for 2018. Members who are electric vehicle users can also now use the AA App to easily find their nearest charging points.



Vehicle and fuel use

We continue to review our vehicles' design and are working to reduce the weight of the racking in the vans to help improve our fuel efficiency MPG further. We are also collaborating with an innovative electric vehicle manufacturer to design and trial a breakdown assistance vehicle to enable us to fully assess the opportunities of this type of vehicle being used within our fleet profile.

Populus Driver Poll Fact

67% support the target to ban the sale of new petrol and diesel cars but 77% say that more needs to be done now to tackle air pollution



Operational vehicles

5% reduction in overall operational fleet emissions

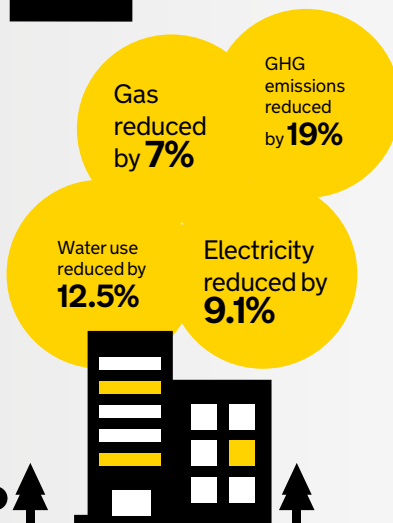
177g/km
Average LCV CO₂ rating down from 181g/km last year



Company car

Average company car CO₂ rating down **from 104 to 89g/km CO₂** compared to last year

42% of our company cars are hybrid or plug in hybrid, up **15%** from last year.



Building energy use

Our programme of energy monitoring and savings initiatives has continued successfully and we have made further significant reductions throughout our offices. We have continued to focus on effective day-to-day energy management within our buildings and during 2017 we have also introduced water management plans in each of our main offices to increase focus on these areas. Investment has also been made in capital projects such as a complete boiler refit at our Newcastle office achieving a 33% absolute reduction in gas usage compared to last year. Over the last five years, we have achieved a reduction of 24% in electricity use and 19% in gas use.

We have made significant improvements in our main offices during the year, compared with our performance in the previous year, as can be seen from the reductions achieved in energy and gas use.

WORLD RECORD FOR MILES PER GALLON



The AA provided official adjudication and supported Honda in a world record attempt – driving 844 miles, between Land's End and John O'Groats on a single tank of fuel. This was a world record for any petrol car, beating the previous record of 71 mpg – achieving an incredible 95 mpg.

6 CLEAN WATER AND SANITATION



Water usage

While we are not a water intensive industry (our water usage primarily extends to normal office functions), we measure our usage and aim to reduce the levels we use per head within our main sites. In partnership with our facilities contractor we have introduced water management plans at our main buildings. We are pleased to report that this year we achieved a 12.5% reduction in our water usage compared to last year. Over the last five years, we have achieved a reduction of 11%.

Waste

zero to landfill

We continue to achieve zero waste to landfill from our main sites.

Summary GHG footprint

The Group's total greenhouse gas emissions for 2017/18 are listed below in tonnes of carbon dioxide equivalent (tCO₂e). The majority of our emissions stem from our operational fleet (88%). Scope 2 emissions are reported for location (country-specific emission factors) and market (energy supplier-specific emission factors). Our footprint encompasses all activities that are material to our environmental impact and include both our fleet and property operations.

GHG emissions

Emissions source	tCO ₂ e 2018	tCO ₂ e 2017	tCO ₂ e 2016	% change
Scope 1 emissions (direct combustion of fuels in stationary and mobile sources, and fugitive emissions)	41,901	44,922	43,740	Decrease 7%
Scope 2 emissions, market-based (emissions from generation of purchased energy in owned or controlled equipment and operations, using a supplier-specific emission factor)	2,920	5,480	7,577	Decrease 47%
Scope 2 emissions, location-based (emissions from generation of purchased energy in owned or controlled equipment and operations, using a regional emission factor)	3,674	4,887	6,514	Decrease 25%
Total emissions (market-based)	44,821	50,402	51,317	Decrease 11%
Out of scope emissions (emissions from the biofuel content in forecourt diesel and petrol)	1,045	996	1,390	Increase 5%
Fleet intensity measurements 1 (tCO ₂ e/job) (emissions from operational fleet divided by the number of operational job tasks completed)	0.01087	0.01122	0.01108	Decrease 3%
Property intensity measurements 2 (tCO ₂ e/ft ²) (market-based emissions from energy use in UK Corporate portfolio (electricity and natural gas consumption), divided by floor area)	0.00703	0.01119	0.01385	Decrease 37%

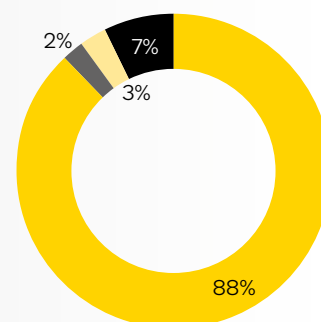
Methodology

Emissions reported as required under Companies Act 2006 (Strategic Report and Directors' Reports) Regulations 2013. Calculations follow the GHG Protocol Corporate Accounting and Reporting Standard (revised edition), using emissions factors from UK Government's GHG Conversion Factors for Company Reporting 2017. Overseas factors have been obtained from national agencies.

The GHG reporting period aligns with financial statements 2017/18. <1% of consumption data is estimated using GHG Protocol guidelines. Boundaries are defined using the operational control approach. Emissions from 'AA The Driving School Agency Limited' are considered out of scope, it operates as a franchise and AA plc has neither equity rights nor control over franchisees. Home-based teleworkers are excluded from GHG reporting.

BREAKDOWN OF EMISSIONS SUMMARY

- Scope 1 Operational Fleet
- Scope 2 Company Cars
- Scope 1 Property
- Scope 2 Property



The AA's commitment to Corporate Responsibility

continued

Our suppliers

Supplier management

The AA understands that the foundations and success of our business are in part due to the quality of our suppliers and the goods and services they provide. We want to work closely and effectively with our supply base so all parties benefit – most importantly our members and customers.

With a focus on our core business value “dynamism”, the Procurement team has identified the need to embrace and deliver more technologically focused third party engagement and management practices. Therefore, we have started the journey of implementing a targeted suite of e-procurement, cloud-based products which will improve the identification and management of risk, increase efficiency and improve performance across our supply chain. This new platform will be delivered over the next 12 months.

A key development of our technological solution is the launch of the AA Supplier Portal which will give suppliers control over their master data and full transparency of the payment cycle. It will enable suppliers to flip purchase orders into invoices and provide the capability to track invoices through to payment, giving them the comfort of knowing when to expect payment. Other benefits to our suppliers include:

- › A more streamlined payment process
- › A reduction in errors and delays
- › A reduction in exceptions

Once fully implemented the AA will have an intuitive, effective and fully auditable system in place, with a host of supplier management information instantly available. Due to the size of this project, this will be undertaken in a phased programme with the aim the majority of our suppliers transacting on the new platform within three years.

Following the AA's Modern Slavery Statement in 2016, a target was set to ensure that 75% of our preferred suppliers sign up to our Supplier Code of Conduct. We are pleased to report that, at the date of producing this report, over 50% have signed up and we are on track to reach the 75% target. Furthermore, all potential new suppliers must agree to the Code before trading can commence.

Contractor management

Home Services contractor management –

The highest gas safety standards have been maintained with no HSE or Gas Safe incidents. Our dedicated team of auditors have audited around 2,000 gas related activities this year across both directly employed and contractor work forces.

Roadside contractor management –

During 2017 our dedicated team has carried out audits covering 84% of our roadside contractors. This has enabled us to verify that they are continuing to provide a high level of service to our customers and are complying to relevant legislation as well as adhering to AA standards.

Data protection and management

As identified earlier in the materiality analysis and in our risk section of this report (pages 34 to 37), data management is a principal risk for the AA and its external stakeholders. We therefore have a system of management in place to mitigate this risk. We have a Data Protection Policy and all employees are required to undertake annual e-Learning on the subject. We also have a number of information security policies to further protect personal data that we hold. During the year we split the Head of Information Security role and employed a separate Data Protection Officer to enhance our focus and ongoing compliance. The Data Protection Officer reports directly to the General Counsel and Company Secretary. Reporting to management occurs for any potential data protection issues. Compliance will be actively monitored by our Data Protection Officer and legal team. We maintain registers of incidents so that we can learn from incidents to help prevent them in the future.

A Group wide GDPR programme is underway to ensure compliance with GDPR by 25 May 2018 and will enhance the Company's governance and management of its customer and employee data. The programme was broken down into multiple workstreams led by a programme director. Each workstream has an individual sponsor for oversight and a project manager was assigned to run day-to-day operations in each workstream. The programme is overseen by an Executive Steering Group chaired by the General Counsel and Company Secretary. An internal audit of the GDPR programme is underway.

Non-financial information statement

We are committed to complying with the new Non-Financial Reporting requirements contained in sections 414CA and 414CB of the Companies Act 2006. The table below aims to help our stakeholders understand our position on key non-financial matters and how we are addressing our reporting requirements.

Reporting requirement	The AA's key policies and standards which govern our approach and controls	Where this is referenced in the report
Environmental matters	Health, Safety and Environmental Policy (E)	Environment (page 44)
	Health, Safety and Environmental Management System (I)	
	Sustainability and Social Responsibility Policy (E)	
	Prevention and Control of Environmental Incidents Policy (I)	
	Waste Management and Minimisation Policy (I)	
Company employees	Business Standards Policy (I)	Principal risks 7 and 9 (pages 35 and 36)
	Terms of Employment and Policy Guide (I)	Board of Directors Diversity (page 41)
	Working Time Policy	Nomination Committee Report (page 64)
	Absence policies including Absence Management, Maternity, Adoption and Family Leave (I)	Our people (page 40)
	Learning, development and performance policies, including Managing Performance, Performance and Development Behaviours (I)	Safety (page 42)
	Equality and Diversity Policy (I)	Our employees (page 20)
	Health, Safety and Environmental Policy (E)	Our community (page 48)
	Health, Safety and Environmental Management System (I)	
	Sustainability and Social Responsibility Policy (E)	
Social matters	Sustainability and Social Responsibility Policy (E)	Our community (page 48)
	Treating Customers Fairly Policy (I)	
	Vulnerable Customers Policy (I)	
	The AA Charitable Trust (UK charity no. 1125119) (E)	
Respect for human rights	Equality and Diversity Policy (I)	Our people (page 40)
Anti corruption and anti bribery	Anti-Money Laundering Policy (I)	Our people (page 40)
	Anti-Bribery and Allowable Gifts, Hospitality and Donations Policy (I)	
	Conduct Risk Policy (I)	
	Conflicts of Interest Policy (I)	
	Financial Crime Policy (I)	
	Insider and share policies, including Insider and Market Abuse, Insider Information Disclosure and Share Dealing Code Policy (I)	
Due diligence and outcome	Whistleblowers Policy (I)	Risk Committee Report (page 67)
	Risk Management Framework Policy (I)	
	Annual Internal Audit Plan (I)	
	Risk Register (I)	
Business model	ISO14001, ISO9001 and OHSAS18001 certification for specified business areas (E)	Audit Committee Report (page 70)
		Our business model (page 5)
Non financial key performance indicators		Key performance indicators (page 22)

I – Group Policies, standards and guidelines that are published internally only

E – Group Policies, standards and guidelines that are published externally on theaapl.com

The AA's commitment to Corporate Responsibility

continued

Our community

Driver distraction

During 2017, The AA Trust continued to focus on the very important safety risk of driver distraction, building further on the success of the awareness campaigns we ran during the previous year.

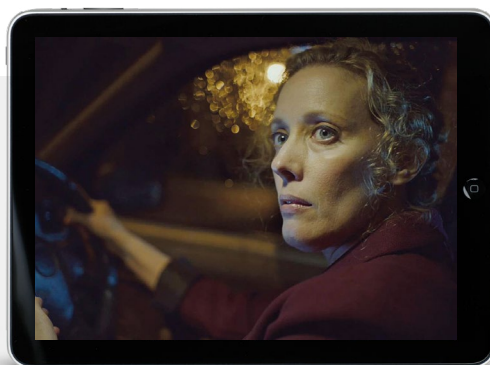
We worked closely with our advertising agency, adam&eveDDB, to make a short advertisement 'Designated Driver' to highlight the dangers of texting at the wheel. This was a hard-hitting approach, using the slogan, 'You are twice as likely to crash text driving as drink driving'. This won several prestigious awards including gold awards at both The British Arrows Awards (UK's most respected marketing awards) and the Clios (leading American/international creative awards).

We continued the campaign in association with the FIA Foundation which included:

- › Hundreds of external posters on bus shelters and ad sites depicting the singer Pharrell Williams
- › Just prior to Christmas releasing a hard-hitting anti-text driving video entitled "Make it home for Christmas". It was made by M&C Saatchi and Mad Ruffian, set to the 1943 Bing Crosby hit "I'll be home for Christmas". It shows a young girl texting her father while he is driving home for Christmas and the consequences of his actions. It received global coverage and appeared on the Today Show in Los Angeles

The full Driver Distraction Campaign #nevertexdrive was also shortlisted for the Broadcast Award at the PRCA Awards.

AA President Edmund King OBE also worked with the Road Safety Minister and Think! Campaign and won their agreement to pay for the distribution of the short advertisement in cinemas and Video on Demand across the UK. The ad was used as the cornerstone of our campaign with the DfT to raise awareness of the new penalties introduced for using a hand-held mobile phone on 1 March 2017. This achieved widespread national coverage from BBC Breakfast TV to BBC Crime Watch. We are grateful to the FIA Road Safety Grant Programme for a contribution of 29,000 euros towards the campaign.



Watch the advert at
theaapl.com

Populus Driver Poll Fact
Almost half of under 35s can't bring themselves to turn their mobile off before driving



THE BRITISH ARROWS 2017 WINNERS – AA CHARITABLE TRUST

Designated Driver
adam&eveDDB's "Designated Driver" picked up several prestigious awards including gold awards at both The British Arrows Awards (UK's most respected marketing awards) and the Clios (leading American/international creative awards).

Populus Driver Poll Fact
76% support installation of EV charging points at garages

Drive Electric

The AA Trust developed a new free course, Drive Electric, to show drivers how to get the best out of driving an electric vehicle. The course is being piloted at the Milton Keynes EV Driving Experience Centre, located in a 4,000 sq ft, state-of-the-art showroom. It will help inform the town's residents and visitors about the benefits of electric vehicle ownership in a relaxed setting. Showcasing the latest EVs from a range of leading vehicle manufacturers, visitors will be able to discuss all elements of owning and running an electric vehicle, as well as having the option to test a range of cars on local roads.



AA campaigns

Smart motorways: We are campaigning for more lay-bys on smart motorways where the hard-shoulder is used as a running lane as we believe safety is compromised.

Street lights: We have raised concerns on some roads where coroners have indicated that turning off streetlights has led to deaths.

Potholes: We campaign for ring-fenced funds to improve the state of the roads and raised the issue highlighted by a coroner that lack of repairs can lead to deaths of cyclists.

Air quality: We have pushed for local authorities to target the 10% of polluters that cause 50% of the issue rather than 'demonising' all diesels.

Cost of driving: We have warned that increases in Insurance Premium Tax could make it unaffordable for many young drivers or lead to more uninsured drivers. We continue to monitor fuel prices with a monthly report.

Changes to the Highway Code: We have written to and met the Road Safety Minister to suggest various changes to the Highway Code to make motorways safer for drivers, recovery workers and the emergency services, following the deaths of two non-AA recovery workers on the hard shoulder.

Caught in a trap: We have sent a dossier to the Transport Secretary on how to improve the enforcement of parking and speeding offences.

Future car: We have promoted the take-up of electric and hybrid vehicles through a partnership with Chargemaster, the leading supplier of electric charging points. AA president, Edmund King OBE, developed a blog on 'Living with an EV' and has spoken at numerous conferences on the issue.

Helping teenagers in care

The AA Trust continues to support teenagers in care in Bristol, Medway, Newcastle and Westminster by helping them learn to drive. The positive effects on self esteem and opening up job opportunities to them are being monitored and findings will be given to the Children's Commissioner and Education Minister.

Populus

Children in Need

Our offices raised over £4,100 which was doubled by us.

Bangers for Ben

We provided official support for the charity rally, providing full breakdown cover for all participants; we even entered our own team!

AA-Populus Driver Poll

The largest dedicated motoring opinion panel in Europe with over 200,000 drivers and members signed up to take part. Around 20,000 take part in the surveys which range from safety issues, environmental opinion and general motoring concerns. These surveys then help drive our campaigns (see AA Campaigns section for more details). Our 112th survey took place in December 2017.

Recycling Lives

We have entered into a partnership with salvage operator Recycling Lives, sending over 7,500 end of life vehicle to them for processing. They provide employment opportunities for ex-offenders (a saving to society of £263,060 a year) as well as using some of their profits to distribute over 30,000 meals to charities and community centres.

C.A.R.S (Changing Attitude on Road Safety)

The programme, funded by the AA Trust, aimed at preventing young people being killed or seriously injured on UK roads, focuses on four main behaviours (speeding, drinking and driving, using your Seatbelt and using your mobile phone). In 2017, we started the roll out of the project, which included coverage on the Road Safety GB website, coverage on London Road Safety Council's website and Facebook group, a pilot with Fire Scotland and finally Birmingham City Council committing to a pilot in their city with plans to roll out on a larger scale.



Governance Report

Compliance with the UK Corporate Governance Code


The AA complied with the principles and provisions of the UK Corporate Governance Code published in April 2016 (the Code) during the financial year ended 31 January 2018 except in the following two respects:

- › During the first half of the year, the roles of Chairman and Chief Executive Officer (CEO) were combined. The dismissal of Bob Mackenzie accelerated the process of separating these roles, which was already in progress. The appointment of John Leach as Chairman and Simon Breakwell as CEO led to compliance with the Code in this regard, during the second half of the year.
- › Following his appointment as Chairman, John Leach remained a member of the Audit Committee during the second half of the year. This was to provide consistency and experience on the Committee, in particular while the process to follow through the change of auditor was implemented. Good progress is being made in the search for additional Board members, which will provide an opportunity for John Leach to step down from his role on the Audit Committee.

The AA expects to be fully compliant with all principles and provisions of the Code as the year progresses.

Leadership


The profiles of our Board of Directors and Executive Committee illustrate our new and revived leadership structure established since the appointment of Simon Breakwell as CEO. Since 1 August 2017, there has been a clear division of responsibilities between the Chairman and CEO. The Board is collectively responsible for the long-term success of the Company. Over half the Board comprises independent Non-Executive Directors (NEDs) and John Leach was considered independent upon his appointment as Chairman. Andrew Blowers was appointed as Senior Independent Director (SID) on 1 August 2017 following John Leach being appointed as Chairman and stepping down from that role.

 Find out more on **P52-55**

Effectiveness

The Nomination Committee report includes explanation of the process for the appointment of the Chairman, Interim CEO, CEO, SID and Remuneration Chair during the year.

The Nomination Committee report also details our first formal externally facilitated Board and Committee evaluation and action plan. The balance of skills, experience, independence and knowledge of the Board is considered regularly as part of succession planning. Time commitments of Directors are considered annually. Induction and ongoing training records are held by the Company Secretary. All Directors will stand for election or re-election by shareholders at the Company's Annual General Meeting (AGM), with the exception of Andrew Miller who will not be seeking re-election following his recent appointment as a Partner of Terra Firma.

 Find out more on **P64-66**

Relations with shareholders


Extensive engagement with, and listening to, shareholders took place during the year and continues on a variety of topics including the Board changes, performance conditions of the Performance Share Plan and the new Remuneration Policy.

The whole Board is expected to attend the AGM on 7 June 2018, except for Cathryn Riley who was appointed in February 2018 and has a previous commitment. Directors will be available to answer shareholders' questions. To facilitate shareholder participation, proxy voting is available.

 Find out more on **P62-63**

Accountability

The Risk Committee report highlights its role in assisting the Board to set the risk appetite and review the principal risks resulting from the strategic objectives. Risk management and internal controls that are applied, are considered to be appropriate.

 Find out more on **P67-69**

The Audit Committee report describes the audit tender process which was undertaken during the year. PricewaterhouseCoopers LLP (PwC) is proposed as our new auditor in respect of financial reports for periods commencing 1 February 2018, subject to shareholder approval at the AGM on 7 June 2018. Our non-audit fees policy, which was reviewed and approved in September 2017, is in place and will continue to be applied and monitored during the change of auditor process.

 Find out more on **P70-74**

The Directors' Report and the Responsibility statement of the Directors are set out on pages 89 to 92 and page 92 respectively.

Remuneration

The new 2018 Remuneration Policy is published with the Remuneration Committee report and will be put to shareholder vote at the AGM on 7 June 2018. The policy includes only minor changes to the policy approved by shareholders in 2015. The Remuneration Report explains the work of the Committee and details the remuneration received by the Directors during the year in accordance with the Policy approved by shareholders in 2015 and in place during the year. The 2015 Performance Share Plan was utilised during the year to make an award to the new CEO and senior executives with options over Ordinary shares. A consultation with shareholders on the performance conditions is underway and the proposed criteria will be published on our investor website. No Director is involved in deciding their own remuneration. Performance Share Plan (PSP) awards have not been valued as at 31 January 2018, as the performance conditions had not been set.

 Find out more on **P75-88**

Chairman's governance overview



We stand today a stronger and more dynamic Board. We remain assured that our strategic focus and strengthened governance will deliver long-term value to our members, customers, employees and shareholders.

John Leach
Chair



Dear Shareholder,

I write to you as Chairman, rather than as SID as in the last three years' reports. The reason behind this change is well known and it has been a difficult year for the AA. However, let me reiterate, it is one in which there is much to be proud.

Conforming to best practice

As stated in our last annual report, the Board had recognised that its composition, with combined CEO and Chairman roles, did not conform to best practice standards and had initiated the recruitment process for a CEO to separate these roles. Subsequently, the decision to dismiss Bob Mackenzie from his role as Executive Chairman on 1 August 2017 accelerated that process and, while the catalyst for this was not what one would have wanted, the result is very positive. Simon Breakwell's appointment has given us a timely opportunity to evaluate our strengths and renewed energy to combat challenges.

Values, attitudes and behaviours

The Board's actions in the case relating to Bob Mackenzie were swift and decisive and it is our continuing responsibility to ensure that the values, attitudes and behaviours we require of all AA employees are constantly reinforced through our leadership, business standards and communication. Our updated strategy, alongside a stronger corporate governance structure and clear corporate values, will transform the success of the AA.

During the 2018 financial year, our key corporate governance actions have been as follows:

1. Board and Executive Committee changes. This is discussed in more detail in the Nomination Committee Report on pages 64 to 66.
2. Our first external Board evaluation review. This is discussed in more detail on page 58.
3. Successful refinancing of the AA Group's near term debt and the senior term and working capital facilities. This was a refinancing project aligned with our strategic objective that reduced interest costs and extended the debt maturity on improved terms. This is discussed in more detail in the Financial review on pages 27 to 31.
4. The oversight and management of regulatory risks across the Company, including implementation of new rules and regulations. This is discussed in more detail in the Risk Committee Report on pages 67 to 69.
5. Completion of our audit tender process and proposed appointment of PwC as the AA's external auditor. This is discussed in more detail in the Audit Committee Report on pages 70 to 74.

Having spent nearly four years on the Board, I have been aware of our collective strength and the duty we all take very seriously to protect and build on the AA's notable heritage and brand. We are a stronger and more dynamic Board. We remain assured that our strategic focus will strengthen our operations and will deliver increased long-term value to our members, customers, employees and shareholders.

Our compliance with the required regulatory and statutory standards for a premium listed company is reflected throughout this governance report.

John Leach
Chairman

16 April 2018

Board of Directors



John Leach Chairman

Appointment: John joined the AA as a Non-Executive Director in June 2014 and was appointed as Senior Independent Director on 13 November 2014. John was appointed as Chairman on 1 August 2017.

Responsibilities: As Chairman, John provides leadership of the Board and delivers objective insight and critical debate to Board discussions on strategic and financial matters. As Chairman, he promotes the highest standards of corporate governance and meets regularly with the Non-Executive Directors to discuss governance matters. John is Chair of the Nomination Committee and a member of the Remuneration, Risk and Audit Committees.

Career and experience: John has served on public company boards as either Chairman, CEO or CFO for the past 37 years. He has considerable experience in turnaround situations in the industrial and service sectors sitting on the boards of, among others, Brent Walker (including William Hill and Pubmaster), Myson Group and Luminar. Most recently, John was CEO of Hermes UK Focus Funds and a supervisory Board member of Dometic AB. John began his career as an Articled Clerk and subsequently as a Partner in a firm of chartered accountants. He is a Fellow of the Institute of Chartered Accountants and a Fellow of the Association of Corporate Treasurers.



Simon Breakwell Chief Executive Officer

Appointment: Simon joined the AA in September 2014 as a Non-Executive Director. He was appointed Interim Chief Executive Officer on 1 August 2017 and then Chief Executive Officer on 25 September 2017.

Responsibilities: As Chief Executive Officer, Simon has responsibility for driving and implementing the strategy approved by the Board and has oversight for governance matters.

Career and experience: Simon has significant digital and travel experience. He is currently a Venture Partner at TCV, one of the leading global mid cap funds, and is Chairman of Business Data 4 Travel. Simon is also co-founder of Trover.com and an adviser to Hipmunk.com.

He was a founder of Expedia, a start-up within Microsoft, and ran the North American operations. As President of Expedia International Inc, Simon started up and led the growth of the business in the Europe, Middle East, and Africa regions, including both the Hotels.com and Expedia brands. Simon joined Expedia as a main board Director in 1996 and served for ten years. More recently, Simon was responsible for establishing the European operations for Uber.com.



Martin Clarke Chief Financial Officer

Appointment: Martin joined the AA in June 2014 as part of the MBI team.

Responsibilities: As Chief Financial Officer, Martin has ultimate responsibility for financial planning and overseeing risk management, treasury and internal controls. Additionally, he focuses on investor relations and improving the capital structure of AA plc.

Career and experience: Martin has over 30 years of private equity experience, most recently in the role of Partner and Global Head of Consumer for Permira which he joined in 2002. Prior to Permira, Martin worked at Cinven and Silverfleet, the private equity arm of Prudential plc. He has led a number of major transactions and has sat on the boards of several leading companies including New Look, Gala Coral and Galaxy Entertainment Group, which is listed on the Hong Kong Stock Exchange.



Suzi Williams Non-Executive Director

Appointment: Suzi joined the AA in October 2015 as a Non-Executive Director.

Responsibilities: As Non-Executive Director, Suzi provides objective insight and critical debate to Board discussions on strategic, financial and governance matters. Suzi became Chair of the Remuneration Committee on 1 August 2017 and is a member of the Risk and Nomination Committees.

Career and experience: Suzi has extensive experience with consumer-facing companies and brands. A Procter & Gamble trained brand marketer and business leader, Suzi has spent the last 20 years delivering commercial transformation and growth for household names like the BBC, Orange and Capital Radio Group (where she was Commercial Development Director at Global Radio Group from 2004 to 2006). In September 2015, after a ten-year tenure, she stepped down from her role as Group Marketing and Brand Director at BT plc.



Mark Millar/Nadia Hoosen General Counsel and Company Secretary

Responsibilities: The Company Secretary is responsible for corporate governance matters, working closely with the Chairman, SID and Board of Directors. They attend all Board and committee meetings. They lead legal and regulatory aspects of the AA's business and transactions, such as the financial restructuring projects and the sale of the Home Emergency Services business.

Mark Millar

Appointment: September 2014.

Retired: April 2018

Career and experience: A qualified solicitor, Mark was formerly Company Secretary at Domino's Pizza Group plc and Future plc and has 15 years of experience in the role. Mark also has a wealth of commercial and legal expertise, including ten years as a City solicitor, latterly with Allen & Overy. Mark leaves the AA to return to private legal practice in April 2018.

Nadia Hoosen

Appointment: July 2018.

Secretary Appointment date: July 2018

Career and experience: As a qualified solicitor, Nadia has 16 years of legal and regulatory expertise, and spent the last 11 years of her legal career in house within regulated consumer facing, technology, media and telecommunications environments at FTSE 250 companies. Nadia is currently Group Legal Director & Deputy Company Secretary at TalkTalk Telecom Group plc, she also held positions at The Carphone Warehouse Group plc prior to its merger with Dixons Retail plc.



Andrew Blowers Senior Independent Director

Appointment: Andrew joined the AA in September 2014 as a Non-Executive Director and was appointed as Senior Independent Director on 1 August 2017.

Responsibilities: As Non-Executive Director, Andrew provides objective insight and critical debate to Board discussions on strategic, financial and governance matters. Andrew is Chair of the Risk Committee and a member of the Audit and Nomination Committees. Andrew is Chair of AA Underwriting Insurance Company Limited, the Group's insurance underwriter.

Career and experience: Andrew has significant experience in insurance and financial services. He established and sold several successful insurance operations during his 25-year career in the insurance industry, the last being the innovative online insurer Swiftcover, and he was previously an Executive Director of Churchill Insurance. He has previously advised several private equity operations, the Consumers' Association and the Financial Ombudsman Service in relation to various insurance matters. Andrew was awarded an OBE in 2009. Andrew is a Non-Executive Director of Telecom Plus plc.



Andrew Miller Non-Executive Director

Appointment: Andrew joined the AA in June 2014 as a Non-Executive Director.

Retirement: Andrew will not seek re-election at the AGM on 7 June 2018.

Responsibilities: As Non-Executive Director, Andrew provides objective insight and critical debate to Board discussions on strategic, financial and governance matters. Andrew is Chair of the Audit Committee and a member of the Risk and Remuneration Committees.

Career and experience: Andrew is a Partner of Terra Firma. He has extensive experience of successful digital transformation in consumer-facing industries, most recently working with Founders' Forum supporting multinational business on digital transformation. As CEO of the Guardian Media Group from 2010 to 2015, Andrew reshaped the Guardian's portfolio of businesses to support its transformation into one of the world's leading digital organisations. From 2002 to 2014, he carried out a similar transformation as CFO and non-executive director of Trader Media Group, which included Autotrader, in its transition from magazines to a wholly digital company.

Andrew is a member of the Institute of Chartered Accountants of Scotland, qualifying in 1991, and training with Price Waterhouse after completing his law degree at Edinburgh University.



Cathryn Riley Non-Executive Director

Appointment: Cathryn joined the AA plc Board on 28 February 2018 as a Non-Executive Director.

Responsibilities: As Non-Executive Director, Cathryn provides objective insight and critical debate to Board discussions on strategic, financial and governance matters. Cathryn also became a member of the Risk Committee on 28 February 2018.

Career and experience: Cathryn has had a wide-ranging career covering insurance, customer services, IT, operations and human resources. She also holds non-executive roles at Equitable Life, International Personal Finance plc, Chubb European Group Plc and Chubb Underwriting Agencies Ltd. Cathryn was Group Chief Operations Officer at Aviva Plc and a member of the Executive Committee. She was a management consultant at Coopers & Lybrand and General Manager of Transformation at BUPA. Cathryn has been a Non-Executive Director and Chair of the AA Group's insurance broker since December 2014 and at the time of writing, will resign following the appointment of a further Non-Executive Director and a period of handover during 2018.

BOARD AND COMMITTEE ATTENDANCE

Director	Date appointed to Board	Attended/ Max possible				
		Board	Audit Committee	Nomination Committee	Remuneration Committee	Risk Committee
John Leach Chairman (from 1 Aug 2017)	26 June 2014	10/10	4/4	5/5	1/1	4/4
Simon Breakwell ¹ CEO (from 1 Aug 2017)	17 September 2014	10/10	–	3/3	2/2	–
Martin Clarke CFO	26 June 2014	10/10	–	–	–	–
Andrew Blowers SID (from 1 Aug 2017)	25 September 2014	10/10	4/4	5/5	1/1	–
Andrew Miller ² Non-Executive Director	26 June 2014	8/10	4/4	–	3/4	4/4
Suzi Williams Non-Executive Director	1 October 2015	10/10	–	5/5	4/4	4/4
Former Director						
Bob Mackenzie ³ Executive Chairman (until 1 Aug 2017)	26 June 2014	5/5	–	3/3	–	–

¹ Simon Breakwell was appointed Interim CEO on 1 August 2017 and permanently to the role on 25 September 2017 having sat on the Board as a NED since 17 September 2014.

² Andrew Miller will not stand for re-election at the AGM on 7 June 2018.

³ Bob Mackenzie was dismissed on 1 August 2017.

All Board members attended the AGM.

A number of adhoc Board and Committee meetings were held during the year at short notice to discuss specific matters. These meetings are not reflected in the above table.

Where appropriate, members of the senior management team were invited to give presentations at Board meetings.

Key to Committees

A Audit Committee **N** Nomination Committee **R** Remuneration Committee **RI** Risk Committee

Executive Committee



Simon Breakwell
Chief Executive Officer

Appointment: Simon joined the AA in September 2014 as a Non-Executive Director. He was appointed Interim Chief Executive Officer on 1 August 2017 and then Chief Executive Officer on 25 September 2017.

Responsibilities: As Chief Executive Officer, Simon has responsibility for driving and implementing the strategy approved by the Board and has oversight for governance matters.

Career and experience: Simon has significant digital and travel experience. He is currently a Venture Partner at TCV, one of the leading global mid cap funds, and is Chairman of Business Data 4 Travel. Simon is also co-founder of Trover.com and an adviser to Hipmunk.com.

He was a founder of Expedia, a start-up within Microsoft, and ran the North American operations. As President of Expedia International Inc, Simon started up and led the growth of the business in the Europe, Middle East, and Africa regions, including both the Hotels.com and Expedia brands. Simon joined Expedia as a main board Director in 1996 and served for ten years. More recently, Simon was responsible for establishing the European operations for Uber.com.



Martin Clarke
Chief Financial Officer

Appointment: Martin joined the AA in June 2014 as part of the MBI team.

Responsibilities: As Chief Financial Officer, Martin has ultimate responsibility for financial planning and overseeing risk management, treasury and internal controls. Additionally, he focuses on investor relations and improving the capital structure of AA plc.

Career and experience: Martin has over 30 years of private equity experience, most recently in the role of Partner and Global Head of Consumer for Permira which he joined in 2002. Prior to Permira, Martin worked at Cinven and Silverfleet, the private equity arm of Prudential plc. He has led a number of major transactions and has sat on the boards of several leading companies including New Look, Gala Coral and Galaxy Entertainment Group, which is listed on the Hong Kong Stock Exchange.



Janet Connor
Director, Insurance

Appointment: August 2014.

Responsibilities: In March 2018, Janet successfully completed her regulatory conduct responsibilities in respect of the regulatory change agenda and now has accountability for the insurance strategy and growth plan at the AA.

Career and experience: Janet is a Fellow of the Institute of Directors and has pursued a successful career in consumer financial services across retail banking and insurance. Prior to joining the AA, Janet held Managing Director roles in general insurance and latterly she was managing director of RSA plc's brand, More Than. Previous to this, Janet ran Ageas-owned over-50s insurer RIAS from 2006 to 2011. Janet has sat as a Non-Executive Director of Vanquis Bank, Provident Group since April 2017.



Gareth Kirkwood
Chief Customer Operations Officer

Appointment: November 2017.

Responsibilities: Gareth is responsible for leading the Customer Operations function at the Group with a focus towards providing the highest standards of service to our customers.

Career and experience: Gareth spent over 20 years at British Airways, including ten years in procurement, four years as Managing Director of one of BA's Regional Airlines, six years as Managing Director of BA's World Cargo division, and two years as Director of Operations. Since leaving British Airways in 2008, Gareth has worked as Chief Operating Officer of Daisy Group, the UK's largest reseller of unified communications, and as the Chief Operating Officer of Global Navigation Solutions, the world's largest distributor of charts and publications to commercial shipping. Most recently, Gareth led a successful transformation programme in Europe for HomeAway, a division of Expedia.



Mike Lloyd
CEO for Automobile Association Insurance Services Limited (AAISL)

Appointment: September 2014.

Responsibilities: Mike is responsible for the consumer Roadside Assistance, Business Services, Insurance business and Financial Services businesses as well as the marketing, digital and public affairs functions for the AA. In March 2017, Mike became CEO of AAISL (the AA's regulated insurance broking business).

Career and experience: Mike was previously a Partner at Oliver Wyman, leading their consumer services work in the UK.



Mark Millar (Nadia Hoosen from July 2018)
General Counsel and Company Secretary

Appointment: September 2014.

Responsibilities: Mark is responsible for corporate governance matters, working closely with the Chairman, SID and Board of Directors. He attends all Board and committee meetings. Mark leads legal and regulatory aspects of the AA's business and transactions, such as the financial restructuring projects and the sale of the Home Emergency Services business.

During 2016, Mark was awarded the first AA Leadership Award.

Career and experience: A qualified solicitor, Mark was formerly Company Secretary at Domino's Pizza Group plc and Future plc and has 14 years of experience in the role. Mark also has a wealth of commercial and legal expertise, including ten years as a City solicitor, latterly with Allen & Overy.



Edmund King
AA President

Appointment: January 2008.

Responsibilities: Edmund is responsible for public affairs, public relations, campaigns and the AA Charitable Trust.

Career and experience: Edmund has a background in research, media, civil service, commerce and extensive transport campaigns. He has worked in the wine trade in Burgundy and for a radio station in Los Angeles. He has written several reports on transport and often appears as a transport commentator on radio and television. He is also a Visiting Professor of Transport at Newcastle University. He tweets under @AApresident.

Edmund was awarded an OBE for services to road safety in 2016.



Helen Hancock
Human Resources Director

Appointment: May 2012.

Responsibilities: Helen is responsible for delivering the people agenda for the Group and its functions, ensuring appropriate leadership and support is provided for each element of the human resources (HR) strategy. Helen is an attendee on both the AAISL and AA plc Remuneration Committees.

Career and experience: Helen has over 20 years' experience working in HR in medium and large corporate organisations. Prior to joining the AA, Helen worked at British American Tobacco for eight years where she held the role of Head of HR for the Southampton site and senior business partner roles for the Global Product function and Group Research & Development. Prior to this, Helen worked at Aldays Convenience Stores Limited (subsequently acquired by The Co-Op) and B&Q plc with various HR remits.



Ollie Holden
Chief Information Officer

Appointment: November 2017.

Responsibilities: Ollie is accountable for defining and implementing the IT strategy for the Group, shaping the digital transformation and providing robust IT services to customers and employees.

Career and experience: Ollie has highly relevant experience leading change with more than 20 years' IT and transformation experience. As a senior manager within Accenture, he led a number of IT transformation programmes for financial services clients. He has held IT and change leadership positions at LV= and TalkTalk, and has advised numerous companies on the improvement of their IT and change capabilities.

Refined roles and responsibilities

The Board is collectively responsible for the long-term success of the Group. There is a clear division of responsibility between the Chairman and the CEO. The Board meets the Code requirement for more than half of the members to be independent.



Chairman
John Leach

- › Provide leadership of the Board and ensure agendas emphasise strategic, performance and core value creation matters
- › Meet regularly with the independent NEDs to facilitate their development and effective contribution and to address any issues and concerns
- › Ensure that members of the Board receive accurate, timely and high-quality information and that Board decision-making processes are effective
- › Lead the Board in the ongoing monitoring, and annual evaluation of the performance of the CEO
- › Lead and participate in the Board evaluation process and ensure appropriate action plans are put in place and implemented
- › Take the lead in providing a properly constructed, full, formal and tailored induction programme for new Directors
- › Foster relationships founded on mutual respect and open communication between NEDs and management
- › Promote the highest standards of corporate governance, seeking compliance with the provisions of the Code



Chief Executive Officer
Simon Breakwell

- › Provide entrepreneurial leadership of the Company, within a framework of prudent and effective controls which enable risks to be managed
- › Lead the development of the Group's strategic direction and objectives
- › Identify and execute new business opportunities, acquisitions and disposals
- › Review the Group's organisational structure and recommend changes as appropriate
- › Build and maintain effective leadership teams
- › Oversee the Group's risk profile, including the health and safety performance of the Group
- › Lead the Group's corporate responsibility programme
- › Meet with major shareholders on both strategic and governance matters as and when required
- › Ensure effective communications by the Group with its shareholders
- › Ensure the Group complies with its regulatory obligations and ensure good links between the Board and the independent boards of the regulated subsidiaries
- › Ensure the Board is alerted to forthcoming complex, contentious or sensitive issues affecting the Group



Senior Independent Director
Andrew Blowers

- › Act as a sounding board for the Chairman and a trusted intermediary for the other Directors
- › Be available to shareholders if they request contact both generally and when the normal channels of Chairman, CEO or CFO are inappropriate
- › Maintain contact with major shareholders to understand their issues and concerns and attend meetings where necessary to listen to their views
- › Support the Chairman in ensuring the Board are aware of the views of major shareholders
- › Meet with the NEDs without the Chairman present at least annually and lead the ongoing monitoring, and annual evaluation of the Chairman



Chief Financial Officer
Martin Clarke

- › Recommend to the Board an annual budget and financial plan
- › Examine all trade, investments and major capital expenditure proposed by Group companies
- › Oversee risk management, treasury and internal controls
- › Ensure effective communication with shareholders and key stakeholders and updating institutional investors on the business strategy and financial performance
- › Recommend to the Board appropriate changes to the capital structure and debt levels
- › Maintain relationships with the Group's banks and manage the investment and banking portfolio
- › Manage the Group's risk profile including the health and safety performance of the Group
- › Implement the decisions of the Board and its Committees
- › Build and maintain effective leadership teams
- › Ensure the Board is alerted to forthcoming complex, contentious or sensitive issues affecting the Group
- › Identify and execute new business opportunities



Non-Executive Directors
Andrew Miller, Cathryn Riley
and Suzi Williams

- › Constructively challenge and help develop proposals on strategy and empower the Executive Directors to implement the strategy
- › Bring independence, impartiality, experience, special knowledge and a different perspective to the Board
- › Provide guidance on matters of concern and strategy development
- › Oversee risk management and internal controls
- › Protect shareholder and stakeholder interests
- › Scrutinise the performance of the Executive Management in meeting agreed goals and objectives and monitor the reporting of performance
- › Uphold high standards of integrity and support the Chairman and Executive Directors to instill the appropriate culture, values and behaviours in the Boardroom and throughout the Group



Company Secretary
Mark Millar/Nadia Hoosen

- › Develop, implement and sustain high standards of corporate governance
- › Support the Chairman and other Board members as necessary
- › Advise the Board on legislation, regulation and corporate governance developments which impact the Group, and maintain the Group's Corporate Governance Manuals
- › Ensure good links between the Board and the independent boards of the regulated subsidiaries
- › Communicate with shareholders and keep the Board informed of shareholder opinions
- › Coordinate the induction of new Directors
- › Ensure compliance with statutory and regulatory requirements
- › Review and monitor the Group's Remuneration Policy

Our Board in 2018 and beyond

Composition of the Board

The skills and experience of our Board members is broad and has been gained over many years from different environments, such as private equity, entrepreneurial start-ups, strategic consulting and consumer services. All of their careers have involved the delivery of substantial change through operational, financial, strategic or marketing initiatives. The Board is united in its energy and commitment to delivering the objectives of the AA transformation project and building long-term value for shareholders.

Following the change of leadership, the skills and experience of each of the members of the Board has been reviewed. Together, the Board members combine to create a composition that is strongly and appropriately aligned with the AA's values, strategic objectives and corporate responsibilities. We firmly believe that each Board member's experience, gained through previous roles and any current external roles, strengthens the composition of the Board and creates invaluable insight and diversity of thought, and thus has strengthened governance. The Board considers that each member brings strong independent oversight.



Strategic progress

Progress against strategy is discussed at each scheduled Board meeting to closely monitor strategy implementation by the Group. The two-day strategy session held away from the office on 6 and 7 December 2017 provided the opportunity for more relaxed, free-flowing discussion around a broad range of strategic issues. This provided a unique and specific opportunity to develop strategy, address current issues and seek to improve the performance of the business. The sessions focused on the early development of plans by Simon Breakwell for the next three years of development for the business. The NEDs were able to share their expertise and provide independent oversight to the direction of the business. Discussions focused not only on the business plan but also on the individuals leading and implementing that plan. These, and other teams that support them, are key to the delivery of the Board's objectives.

The Board then met again on 20 February 2018 to finalise the strategy. The new business strategy was presented to the market on 21 February 2018. This included plans to innovate and grow the Roadside business and invest to accelerate the growth of the Insurance business.

See Our strategy on pp12-17

Non-Executive Director change

We were pleased to announce the appointment of Cathryn Riley to the Board in February 2018, after the 2018 financial year end. This appointment has further strengthened the knowledge of the Board. We are sorry to lose Andrew Miller, who will not be seeking re-election at the 2018 AGM following his recent appointment as a Partner of Terra Firma. We thank him for his contribution and support during the past four years.

Company Secretary changes

We are sorry to lose Mark Millar as Company Secretary this Spring and wish him well in his return to private legal practice. We are delighted that Nadia Hoosen will join us in July 2018 and will have a period of handover with Mark to ensure a smooth transition.

KEY BUSINESS AT MEETINGS DURING THE 2018 FINANCIAL YEAR

Strategy

- > Two-day strategy session held away from the office, took place in December 2017
- > Board received presentations on a number of key areas, including IT transformation, membership growth and the brand
- > Approved the sale of the Home Emergency Services business
- > New strategy announced in February 2018

Governance and risk

- > Undertook first external Board evaluation, reviewed outcome and produced action plan
- > Recommended appointment of PwC as auditor to the Company with effect from financial year to 31 January 2019
- > Considered emerging risk factors including General Data Protection Regulation (GDPR) and Brexit
- > Received an update on multiple cover
- > Commissioned a property audit to ensure AA buildings were not affected by cladding issues, following the Grenfell fire
- > Received training on Market Abuse Regulations, conflicts of interest and financial crime
- > Reviewed and approved the new CSR strategy

Shareholder engagement

- > CEO and CFO met with shareholders following strategic update
- > Reviewed 2017 AGM proxy figures
- > Received regular updates on Investor Relations (IR) issues
- > Shareholder consultation in response to significant vote against AGM resolution
- > Investor roadshows

Leadership and people

- > Executive Chairman dismissed from post
- > Appointed John Leach as new Chairman
- > Appointed Simon Breakwell as CEO
- > Appointed Andrew Blowers as SID
- > Reviewed organisational structure
- > Restructured the UK Pension scheme
- > Reviewed results from employee engagement survey and produced an action plan

Financial performance

- > Received regular updates on business performance
- > Undertook refinancing in July 2017
- > Monitored adherence against the 2018 budget
- > Approved the 2019 budget
- > Reviewed dividend policy



Plan for 2019: Looking forward to the 2019 financial year, the Board will focus on the following matters:

- > Implement new strategic priorities announced February 2018
- > Implement action plans from engagement survey
- > Seek compliance with GDPR
- > Progress recommendations from the external Board evaluation
- > Manage a smooth transition to the new audit firm
- > Continue to review Board composition

Board evaluation, induction and training

Board evaluation

The Board recognises the need to maintain its development and continually strengthen Board processes. This involves a continuous process of:

- › Reflecting on past performance and implementation of previous recommendations or actions
- › Consideration of future training, skills and diversity requirements
- › Identification and implementation of new recommendations or actions to improve performance

An assessment of the effectiveness of the Board and Committees was conducted in accordance with the guidance in the Code. Condign Board Consulting (Condign) undertook an external Board evaluation review during the year. A detailed and thorough tender process was undertaken during the 2017 financial year which led to the appointment of Condign, an independent external consultancy with no other connections to the Company.

Condign based the review on face-to-face interviews with the Directors, the Company Secretary, Chair of the Insurance subsidiary and senior management including the Human Resources Director. Prior to their interview, each individual was provided with a guide designed to assist with preparation for the topics to be discussed. In addition, Condign attended the Board meeting in September as an observer and reviewed outputs from previous internal evaluations as well as a number of Board packs.

The 2017 Board evaluation focused on the following areas of its role and performance:

- › Board functionality, dynamics and engagement
- › Board organisation, operating rhythm and materials
- › Board engagement with strategy development
- › Shareholder engagement and alignment
- › People and culture
- › Relationship with the Insurance board and the Financial Conduct Authority (FCA)
- › Board Committees
- › Investigation of the circumstances surrounding the dismissal of Bob Mackenzie

The Board evaluation process took place following the dismissal of Bob Mackenzie. This provided an early opportunity to gain an external view of how the new Board positions were operating following the separation of the Chairman and CEO roles. Condign concluded that separation of the role had produced immediate improvements to the effectiveness of the Board.

In November 2017, Condign presented a report to the Board on the findings of the effectiveness review. Following consideration of the findings of this review, the Directors concluded that they remain satisfied that the Board and each of the Board Committees are operating effectively.



The Board reviewed the feedback from the evaluation and produced the following action plan:

- › Facilitate further engagement between the various elements of the Board: Chairman, CEO, NEDs and CFO
- › Provide additional opportunities for the NEDs to participate in site visits, e.g. call centres
- › Increase the number of preparatory and teach-in sessions to aid Board development and understanding
- › Invite external guests to provide an alternative perspective to mitigate the risk of a future 'board bubble'
- › Consider NED succession planning
- › Undertake a second strategy session focusing on people and capacity
- › Further develop the strength of the Executive Committee
- › Develop a greater line of sight between the Board and Executive Committee
- › Ensure that succession planning at senior executive level is strengthened
- › CEO and Chairman to strengthen their understanding of shareholder views and concerns
- › Undertake a formal consideration of the learnings regarding the dismissal of Bob Mackenzie, for the business and the Board
- › Develop a better understanding of the drivers and regulatory needs of the insurance business

The Board have already implemented a number of the actions from the plan, including developing the strength of the Executive Committee, through the appointment of a Chief Customer Operations Officer and a Chief Information Officer. The appointment of Cathryn Riley in February 2018 has further strengthened the knowledge of the Board, in particular their understanding of the insurance broking business.

Progress on these actions will be considered as part of the next performance evaluation and reported on in next year's Annual Report.

Effectiveness of the Chairman

The effectiveness of John Leach as Chairman was considered as part of the Board evaluation process. The feedback provided in the questionnaire was followed up later in the year with one-to-one meetings where responses were discussed with the SID and Company Secretary. The results of the review and subsequent discussion were unanimously positive. The review confirmed that the Board is satisfied that the Chairman is fulfilling his duties and wish him to continue in the coming year and thanked him for stepping in at short notice.

Induction: Simon Breakwell

A tailored induction programme facilitated by the Chairman and the Company Secretary was agreed for Simon Breakwell, following his appointment as CEO. This programme was designed to provide comprehensive information about the AA and its businesses to complement and build on the knowledge Simon had developed as a NED. As a former NED, Simon Breakwell was well known to the Board and many of the senior executives. He also had a good understanding of the Company's governance and regulatory framework, as well as its history. The programme was therefore tailored to ensure that Simon's induction concentrated on areas for which he required greater focus, in depth knowledge and supplemental information. Simon met with senior executives and function heads to gain a greater understanding of the organisation, in particular the progress made on the IT transformation programme and the operation of the insurance business. He received training in a number of governance areas including Directors' duties, conflicts of interest, financial crime and the Market Abuse Regime. He also met with major shareholders and key stakeholders, including the external auditors and FCA.

Simon undertook an extensive exercise to meet a significant number of employees at all levels of the business and across multiple sites. He has met over 2,000 employees by regularly travelling around the AA's major office locations, including the Head Office in Basingstoke and the offices at Oldbury, Newcastle and Cheadle.

Simon has made a particular effort to meet a large number of the Patrol team by attending their regular meetings, as well as joining employees 'on patrol'. He attended the employee awards ceremony and was introduced to both the Patrol of the Year and the Recovery Patrol of the Year.

Induction: John Leach

John Leach had been the SID for two and a half years when he was appointed as Chairman. John's induction programme therefore concentrated on introducing himself to key shareholders in his capacity as Chairman and developing a greater understanding of governance matters.

Training

Members of the Board are provided with regular training in order to keep them abreast of industry and legal and regulatory developments, facilitated by professional advisers where appropriate. During the year the Board was provided with an update on the Market Abuse Regulations following their introduction in 2016. This reminded them of the implications both for them as individuals and for the Group as a whole. The Board also received training on the legal implications of the GDPR prior to the implementation in May 2018 as well as financial crime, conflicts of interest and legal privilege.

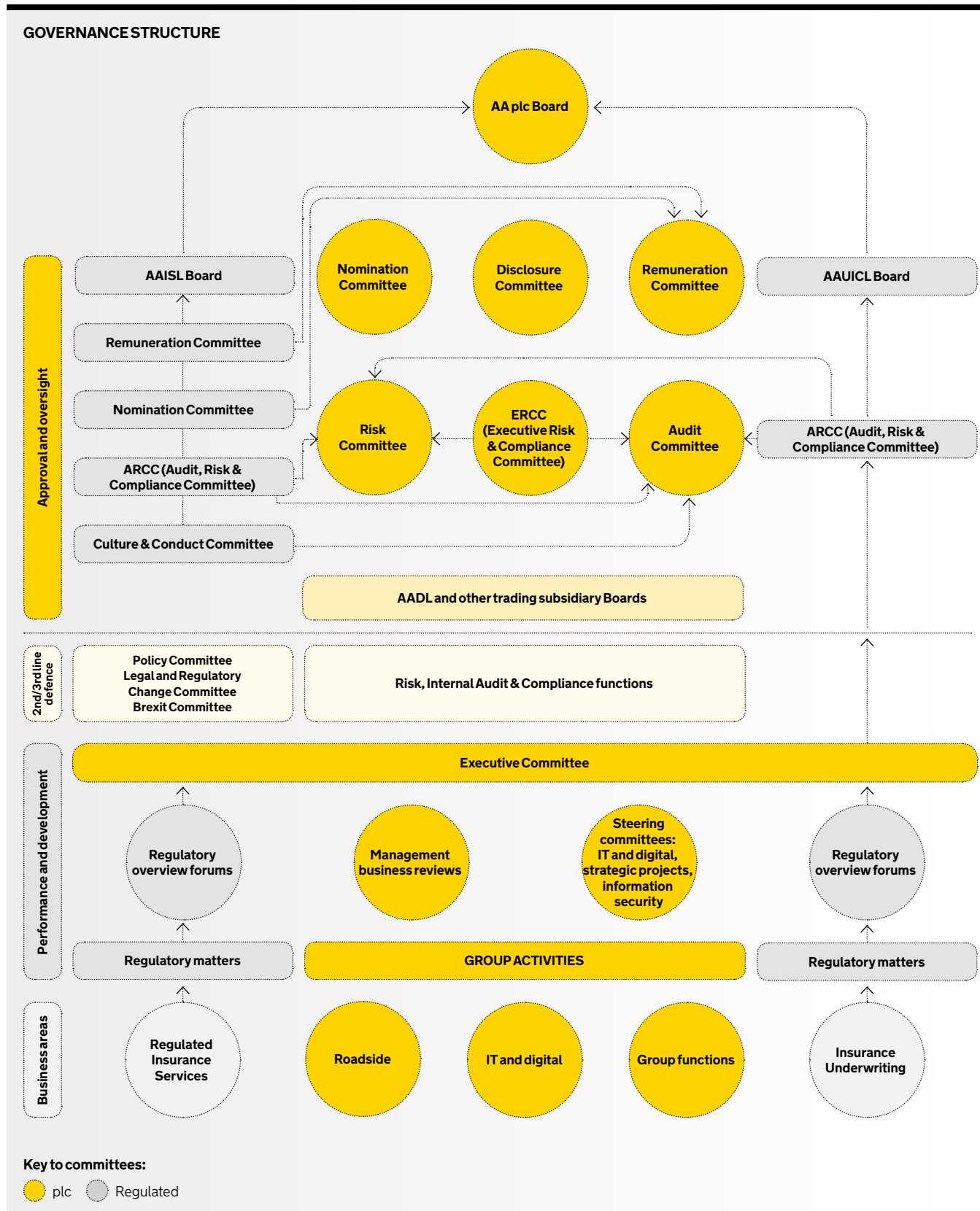


› Simon Breakwell has met over

2,000

employees by meeting patrols and travelling around the AA's major office locations

Our governance structure



The governance structure of the AA Group has evolved since our Initial Public Offering (IPO) in 2014 to provide additional oversight on transformation projects and investment decisions, to meet revised statutory and regulatory requirements and to ensure that our regulated businesses have similarly robust governance standards. This governance structure is critical to ensuring that all our business decisions, operations and activities are carefully scrutinised and controlled so as to safeguard the long-term health and reputation of the AA.

Our governance structure aims to enable appropriate, effective decision making with clear accountabilities. It sets out how the business is managed and operated at all levels and across all business areas. It aims to ensure that the risk profile reflects the strategic objectives of the business, with the ultimate aim of protecting the business from reputational or operational damage. This structure dovetails with the governance arrangements of the regulated subsidiaries in the Group.

A key principle of the structure is the delegation of operational management to the Executive Committee with a matrix of authorities setting out how this is further delegated through the organisation.

The Executive Committee gives strategic focus and is responsible for managing the operational and financial performance of the Group by coordinating the work of the specialist business areas. This enables the efficient and effective day-to-day operation of the Group's businesses.

The Board is kept up to date with developments in the business, including the work of the leadership teams, through regular reports from the CEO and CFO, which are discussed in detail at each Board meeting. Sufficient time is given both before and at the end of each Board meeting for the Chairman to meet privately with the SiD and NEDs to discuss any matters.

Automobile Association Developments Limited (AADL), a subsidiary of the Company, is the entity responsible for the provision of our core Roadside Assistance delivery.

Regulated activities

A number of the Group's businesses include regulated activities and the Group has several regulated subsidiaries. The main such subsidiaries are: (i) AAISL, which runs our insurance broking business and has a board

including three independent NEDs and (ii) AA Underwriting Insurance Company Limited (AAUICL), which is our Insurance Underwriter and has a board including three independent NEDs, chaired by Andrew Blowers, an AA plc NED. The Board works closely with the AAISL and AAUICL boards to ensure that appropriate governance is followed in respect of all regulated Group activities.

The role of the Board

The Board is responsible for the stewardship of the Company, protecting the AA heritage and creating sustainable value for our shareholders. It carries out this role through a range of activities which require strong vision, leadership, entrustment and oversight.

The Board embodies the standards and behaviours of the AA that underpin the delivery of long-term success, and it ensures that the procedures and processes are in place to ensure that these values are well understood and observed. The AA's values, as determined by the Board, are Courtesy, Care, Collaboration, Expertise and Dynamism.

The Board sets the strategy of the Group and provides guidance and oversight to the business operations that assume responsibility for implementing the resulting strategic actions. It agrees the risk appetite and tolerances of the Group and ensures that the risk management structure is aligned and effective. The Board oversees the financial performance of the Group and is also responsible for corporate governance and setting the tone from the top.

Matters reserved for the Board

A number of key decisions and matters are reserved for the Board's approval.

These include:

- > Matters relating to the Group's strategy
- > Approval of major acquisitions, disposals and capital expenditure
- > Monitoring current trading against previously reported trading
- > Matters relating to financing and refinancing
- > Approval of financial results and overseeing the Group's system of internal control
- > An annual Board effectiveness evaluation
- > Setting the Group's risk appetite and the Risk Management Framework

Matters requiring Board and Committee approval are submitted to the Board, or relevant committee, together with supporting documentation, as part of the Board or committee papers. At each Board meeting, the Board pack includes updates from the CEO and CFO and contains financial results and other functional updates. There are presentations on the Company's operations and regular discussions on strategy, marketing, shareholder matters, employee engagement, health and safety, corporate responsibility and governance matters.

A Schedule of Matters Reserved for the Board's decision and clear Terms of Reference for its principal committees, can be found on the Company's Investor Relations website at www.theaapl.com/investors/corporate-governance/board-and-committee-terms-of-reference.

The role of the Committees

The Board delegates certain responsibilities to its principal committees to assist it in carrying out its functions of ensuring independent oversight. Our principal Board committees' constitutions include only independent NEDs and play a key role in supporting the Board. A detailed report on the activities undertaken by each Committee in the 2018 financial year is given by the relevant Chair later in this report.

The Board delegates the implementation of strategy and day-to-day management of the Group's operations to the Executive Committee. The Board delegates oversight of certain of its announcement obligations including under the Market Abuse Regulations to the Disclosure Committee and oversight of share allotments to the Allotment Committee, which was established during the year.

Nomination Committee **P64 to 66**

Risk Committee **P67 to 69**

Audit Committee **P70 to 74**

Remuneration Committee **P75 to 88**

Relations with shareholders

Our approach to investor relations

The Board acknowledges that it is managing the AA on the behalf of shareholders and, in undertaking this responsibility, seeks to increase long-term shareholder value while advancing the interests of all the AA's stakeholders. It recognises that this year has been a tough one for shareholders and the importance of its relationships with shareholders and is committed to maintaining an open dialogue with them and, more generally, the financial community.

We engage with analysts, shareholders and potential investors to ensure we have strong relationships which allow us to understand their views on material issues relating to the business. A critical part of this open dialogue is communication about our strategy and its delivery.

The AA has a comprehensive IR programme which aims to help existing and potential equity and debt investors understand what we do, our strategy and our achievements.

The Board receives independent feedback on our relationships with investors from our brokers. These are included in regular Board reports on IR. All analysts' notes are circulated to the Board to help it maintain an understanding of markets' perceptions of the Company and their financial expectations.

Relevant information made available to investors

Financial reporting

The AA reports financial results twice a year, at the half year and year end. Following the announcement on the London Stock Exchange via the Regulatory News Service (RNS), presentations are held to explain the results. These presentations are simultaneously webcast and posted on the IR website to enable viewing by those unable to attend in person.

Ad hoc announcements

Ad hoc announcements of material information are made via the RNS and are also available on our IR website to ensure all investors are able to access them.

Annual Report

The Annual Report is published in line with requirements to provide sufficient time in advance of the AGM for feedback to be shared with the relevant Directors.

Website

An IR website, www.theaapl.com, is maintained to facilitate communications with investors. We publish all presentations given to investors, all RNSs and press releases, as well as regulatory and CSR (Corporate Social

Responsibility) documents. We run a notification system to enable investors to sign up to receive all RNS announcements automatically, direct from RNS. Most meeting requests come in direct to IR, but since MiFID II came into force in January 2018, we are considering options for a more visible and easily-accessible means for investors to request meetings with IR without going through our brokers.

Meetings with investors enabled through the IR programme

Institutional shareholders

During the year, the IR team and senior management conducted almost 350 meetings and met or spoke to over 140 shareholders or potential investors. This was significantly higher than the previous year as the AA proactively undertook an extensive engagement programme with the financial community following the dismissal of Bob Mackenzie and the revised earnings guidance during the second half of the year.

On 25 September 2017, the AA appointed Simon Breakwell as permanent CEO. Since his appointment he has met all the largest shareholders and many new and potential holders.

Initial meetings are held with IR but when investors take significant holdings, we aim to ensure that investors meet at least one of the Chairman, CEO or the CFO.

Individual shareholders

Individual shareholders are encouraged to communicate with the Directors through the Group Company Secretary.

Bondholders

Meetings with credit institutional investors and analysts were held with senior management and our IR department throughout the year. In addition, regular dialogue was maintained with our key relationship Banks and Bond Trustee.

Credit ratings

During the year, updates and meetings were held in respect of our bonds by our senior management team with credit rating agency Standard & Poor's.

Meetings with the Chairman and the SID

On 1 August 2017, following the dismissal of Bob Mackenzie, the AA announced that John Leach became Chairman and was replaced by Andrew Blowers as SID. John Leach, who had met a number of investors in his role as SID, then met the majority of shareholders and continues to meet shareholders who request meetings. We followed Andrew Blower's appointment as SID with an immediate offer

to major shareholders of meetings with him. He continues, as SID, to be available to meet shareholders. Contact with both the Chairman and SID should be sought through the Company Secretary.

Now that we are through the period dominated by the dismissal of Bob Mackenzie and consequential changes to the Board and new strategy, we will resume our practice of annual discussions between the governance officers of our top shareholders, one or more of the NEDs and the Company Secretary.

Annual General Meeting (AGM)

Investors' views in relation to corporate governance and the Remuneration Policy are sought ahead of the AGM and summarised to the Board.

The 2017 AGM provided shareholders with an opportunity to question the Board and the Chairs of the Board Committees on matters put to the meeting, including the Annual Report. Proxy votes of shareholders for the AGM are counted independently by the Company's registrar, announced at the meeting and published on the Group's website shortly after the conclusion of the AGM.

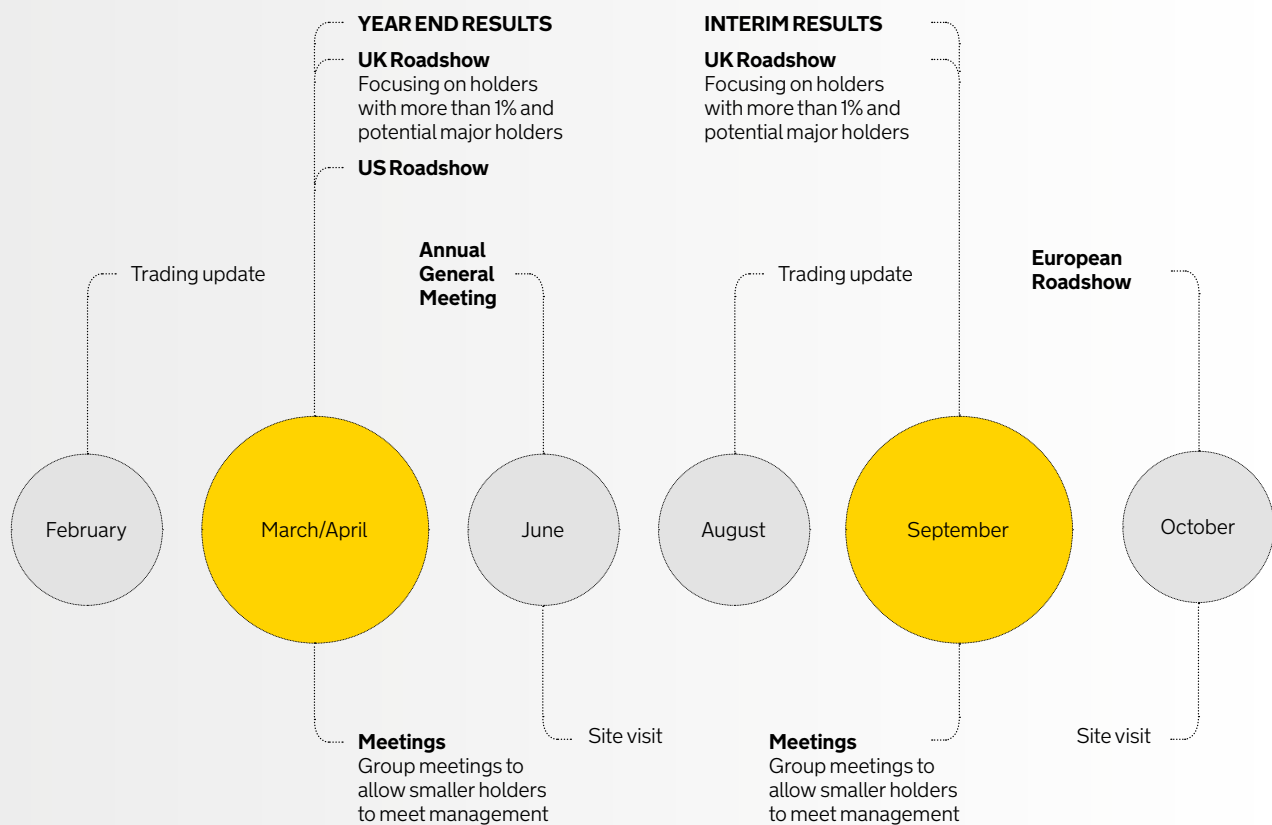
Resolution 16, in relation to a further 5% disapplication of pre-emption rights, was not passed at the 2017 AGM. Resolution 14, which grants authority to allot shares, was passed although a high number of votes were received against it.

A number of the Company's major shareholders have now been consulted in respect of these resolutions. We have been advised that some shareholders generally oppose share issuances with pre-emptive rights above 33% and without pre-emptive rights above 5%. The vote against these resolutions was not specific to the AA. The AA plc share register, however, has a large proportion of its shares concentrated among a small number of shareholders. Consequently, the views of a small number of the shareholders carry a significant weight of votes.

In relation to Resolution 14, shareholders have been consulted on a proposal for the 2018 AGM to separate the resolution for pre-emptive rights above 33% into a separate resolution. This proposal was supported by a number of shareholders.

The 2018 AGM will be held at the offices of Freshfields Bruckhaus Deringer at Northcliffe House, 26-28 Tudor Street, London, EC4Y 0BQ on 7 June 2018.

Investor engagement calendar



The IR calendar is designed to ensure that investors and potential investors get effective access at the appropriate level, while effectively managing senior management time.

In addition to major annual events, we hold multiple one-on-one meetings with IR, senior management and operational management. We include group meetings soon after results to ensure that smaller holders and non-holders

have the opportunity to meet management. We also attend conferences, as relevant, to provide further opportunities for new investors to establish contact.

We offer site visits to our Oldbury operations to allow investors to see the operations and get a feel for the business at a practical level. These are typically held during the summer and we encourage investors to attend as they

gain a valuable insight into our deployment system, spend time with the patrols, observe our call centre operations and meet a range of operational management.

We also conduct presentations with sales teams from those banks which publish research on the AA.

Effectiveness

Nomination Committee Report



The succession planning we had previously undertaken greatly assisted us when swift action was required.

John Leach
Chair of the Nomination Committee



Dear Shareholder,

I am pleased to present the report of the Nomination Committee (the Committee) for the financial year ended 31 January 2018, a very busy year for the Committee. The Committee supported the Board in reviewing its structure and composition, considering diversity at both Board level and throughout the organisation, evaluating its performance and overseeing succession planning for the Board and Executive Committee.

A core focus of the Committee during the 2018 financial year has been to consider key changes to the Board and management, at times in difficult and unforeseen circumstances. The Board also undertook its first external Board evaluation review and agreed a number of key areas to address during the year. The results of this review are detailed on page 58, along with the action plan that will be addressed in the coming year.

The succession planning process for splitting the combined CEO and Chairman roles was a critical piece of work which took place during the year and is set out in detail below. The advanced planning by the Committee greatly assisted our urgent Board change over the summer months. The Board effectiveness review, development of skills matrices and an established talent management programme assisted with the process of understanding the position and prospects of the Board and aided the succession planning process. This report considers this work and the processes in place for the future appointment of any new Director.

The report also sets out other principal activities of the Committee during the year and our plan for the 2019 financial year, including further strengthening the independent Non-Executive Board.

Committee activity during the 2018 financial year

The Nomination Committee undertook the following activities during the 2018 financial year:

- › Reviewed ongoing succession planning for the Board, including splitting the roles of Chairman and CEO and the appointment of further NEDs
- › Considered and recommended candidates in urgent circumstances for the appointment of the Chairman, Interim CEO and SID
- › Considered and recommended candidates for the appointment of a permanent CEO
- › Considered and recommended candidates for the CRO and Company Secretary roles
- › Undertook the first external Board evaluation facilitated by Condign Board Consulting Limited
- › Reviewed the balance of skill, experience, independence, diversity and knowledge on the Board
- › Considered and made recommendations in respect of the constitution of the Board's four main committees
- › Produced a skills matrix of Board members to aid future succession planning and talent management
- › Considered gender and other diversity at Board level and through the management structure
- › Appraised the performance of the Chairman, a process conducted by the SID and NEDs
- › Reviewed feedback from AAISL on its Board evaluation
- › Assessed the future talent pipeline within the Group and senior management succession planning
- › Reviewed the training and development process for Directors
- › Reviewed the time commitments of the NEDs
- › Reviewed the skills and independence of each of the independent NEDs and subsequent recommendation that each of them be elected or re-elected at the Company's AGM to be held on 7 June 2018, with the exception of Andrew Miller who is standing down
- › Reviewed the Terms of Reference of the Committee

The full Terms of Reference of the Committee can be found at <http://www.theaapl.com/investors/corporate-governance/board-and-committee-terms-of-reference>.

Succession planning

Succession planning has been a key focus for the Committee during the current year. As previously indicated it was the Board's intention for Bob Mackenzie's combined role of Executive Chairman to be split during the 2018 financial year. The Committee had started the process of defining the split roles, identifying the skills and experience required for the roles of Chair and CEO. Lygon Group (Lygon) had been appointed to assist with this process.

Before the process was complete, the Committee were informed of a serious incident which involved Bob Mackenzie. Following detailed investigation and consideration of the facts, the Board believed that the appropriate course of action would be to dismiss Bob Mackenzie for gross misconduct and dismissal took place on 1 August 2017. It was therefore necessary for the Committee to expedite the search for both a Chairman and an interim CEO.

Interim CEO

The Committee, in conjunction with the Board, and consistent with our succession plan, approached Simon Breakwell who agreed to take the position of Interim CEO with effect from 1 August 2017.

As a NED, Simon Breakwell had gained a good understanding of the fundamentals of the business. He had significant business experience including as a founder of Expedia and as a venture partner at TCV. The Committee considered his skills and experience, in particular in the digital space, and believed that he would be a good and capable individual to steer the Company through the period of uncertainty and change until the appointment of a permanent CEO was made.

Permanent CEO

The process to appoint a permanent CEO was therefore accelerated in August 2017. A long list of candidates, both internal and external, was formulated. Lygon carried out a due diligence process to identify the most appropriate candidates. This was then narrowed to a short list which included Simon Breakwell. The members of the Committee considered all the shortlisted candidates against a set of criteria which had been agreed in advance. The internal and external shortlisted candidates took part in an interview process.

The Committee was impressed with the work Simon Breakwell had been undertaking as Interim CEO which evidenced his strong leadership skills, integrity, belief in the development of strong culture and values, as well as his ability to influence strategy. It also took soundings from certain major institutional shareholders regarding the potential appointment of Simon Breakwell on a permanent basis. They were all supportive of this proposal. The Committee ultimately recommended Simon Breakwell because they believed that he would be able to build on the progress already made to date and help to ensure that the Company is set up for success in the future.

Non-Executive Director changes

Once the changes to the Board were implemented, the Committee reverted to consideration of Board composition and succession planning in its wider sense. This included succession planning for Directors, NEDs and the senior management team. The Committee also considered the identification of new talent and the review of training plans to prepare individuals for future roles.

Following the Board changes, the Committee reviewed the composition of the Board. It was considered appropriate for the Board to seek additional NEDs. We commenced a search for another director with insurance experience, as well as technology and audit experience. I was delighted that Cathryn Riley, the Chair of the Group's insurance broker, Automobile Association Insurance Services Limited, and former Group Chief Operating Officer at Aviva plc agreed to join the Board in February 2018.

Following the decision by Andrew Miller to step down at this year's AGM, the Board is advanced in the process of finding a new NED to be a replacement as Audit Chair. We are sorry to lose Andrew as a NED and thank him for his service and support to the Board during the past four years.

The Committee recognises the key role that its previous succession plans had in ensuring a smooth transition upon the departure of the Executive Chairman in unforeseen circumstances and accordingly will continue to ensure that there are sufficient succession plans in place for all executive and non-executive positions throughout the Group.

Diversity

The Board's policy recognises the importance of diversity at Board level and throughout the Group and is committed to ensuring that this remains a central feature of the Board and our senior management team. In the interests of the business and our shareholders, the Committee continues to ensure that the business benefits from a representative Board and workforce with a diverse range of skills, experience and knowledge.

Nomination Committee Report

continued

We are committed to increasing the representation of women on the Board and aim to develop a clear plan to achieve Lord Davies' extended target for Women on Boards of 33% female membership by 2020. Diversity charts showing male and female representation at Board, Executive Committee, Leadership and All Employees level are located on page 41 of this report. As at 31 January 2018, female representation was 17%. The recent appointment of Cathryn Riley as a Non-Executive Director enhances the Board's gender diversity.

All aspects of diversity, including ethnic representation, are considered at each level of the recruitment process. The AA supports the recommendations of Sir John Parker's review increasing ethnic diversity at Board level, developing candidates for Board positions and enhancing transparency and disclosure. At each search firm appointment, it has been requested that diversity should be a factor in ensuring a broad candidate pool from a long list. These changes can only be achieved by either an additional appointment to the Board or replacement when another Director steps down, which was necessary during the past year but in a pressing situation. The Board will actively consider this during the coming year.

To achieve these targets, the Committee is working closely with the Human Resources Director to develop clear recruitment plans which recognise the need to increase the diversity of the Board, while being mindful that appointments are made on merit.

Further information on gender and diversity can be found in Our people on page 41.

The Committee's plan for the 2019 financial year includes:

- > Implement actions from the 2018 Board performance evaluation, including the provision of site visits for Board members
- > Recruit further NEDs following the changes in Board roles
- > Undertake work on succession planning for the Board and key roles across the business
- > Progress diversity action plan – to ideally meet Lord Davies' target of 33% women on the Board by 2020 and the recommendations on ethnic diversity made by Sir John Parker in his 2017 report
- > Continue to operate the successful mentoring programme with the senior management team
- > Develop and deliver training and induction programme for the Board and senior management
- > Consider the skills, availability and performance of each Board member and reflect those results in recommendations on the election and re-election of Directors at the Annual General Meeting



John Leach
Chair of the Nomination Committee

Appointment of the Chair, SID and Remuneration Committee Chair

When considering the appointment of a Chair, the Committee agreed that John Leach, as SID, was the appropriate choice for the position. He had led the Board through a difficult period and the Committee believed that he had the necessary attributes and experience required to fulfil the role of Chairman. The Board was unanimous in its view that John was the right person to be Chairman and the appointment was made with effect from 1 August 2017.

John's appointment as Chairman led to a vacancy on the Board for a SID. Andrew Blowers has significant experience in the financial services arena and as a NED. The Committee believed that he would be a very suitable individual to take on the role of the SID.

Before he became CEO, Simon Breakwell was Chair of the Remuneration Committee. His appointment as CEO created a vacancy. Suzi Williams has a wealth of commercial experience and had served on the Committee since her appointment in November 2015 and it was considered appropriate that she should replace Simon Breakwell as Chair of the Remuneration Committee.

None of the Directors participated in discussions about their own appointment.

Accountability

Risk Committee Report



Our risk management framework has been of great significance and help during a challenging year for the AA.

Andrew Blowers
Chair of the Risk Committee



Dear Shareholder,

I am pleased to present the report of the Risk Committee (the Committee) for the financial year ended 31 January 2018.

Effective risk management is a core part of AA governance and culture. Over the last year, the Committee has ensured that the Risk Management Framework and our agreed risk appetite continue to be appropriate for the AA as the transformation initiatives are rolled out. The Committee plays a key oversight role for the Board and this report is presented to demonstrate our approach to risk control and accountability. It sets out the activities and initiatives that we have undertaken during the 2018 financial year and our plans for the forthcoming year.

Supporting the Committee is an Executive Risk and Compliance Committee (ERCC) which meets frequently throughout the year. This is an executive body, made up of senior executives and functional experts. Its role is to implement the Risk Management Framework, highlight exceptions to our risk appetite, understand the root cause of control failures and oversee corrective actions. There is also an Audit, Risk and Compliance Committee (ARCC) for the regulated Insurance broking subsidiary, AAISL, and an ARCC for the in-house underwriter, AAUICL, which also report to the Committee in respect of their work.

I am pleased to report that an experienced Chief Risk Officer has recently joined the Group who will further strengthen the risk and compliance capability within the AA. The Committee works closely with the ERCC, ARCCs and Chief Risk Officer and invites executive members of the Group to attend or present, as appropriate.

Committee roles and responsibilities

Overall responsibility for overseeing the management of risks, compliance with our Risk Management Framework and the agreed risk appetite of the Group lies with the Board. These responsibilities are delegated to the Executive Directors of the Board for the day-to-day management of risks and the process is monitored by the Committee (working alongside the Audit Committee) each of which reports to the Board.

The Committee is concerned with the business of the entire Group and its authority extends to all relevant matters relating to the Company and its business units and subsidiaries. The Committee advises the Board on the Group's overall risk appetite, tolerance and strategy, and oversees and advises the Board on the current risk exposures of the Group and future risk strategy.

Cathryn Riley joined the Committee upon appointment to the Board on 28 February 2018, after the end of the financial year.

Full Terms of Reference of the Committee can be found at <http://www.theaapl.com/investors/corporate-governance/board-and-committee-terms-of-reference>

Risk Management Framework

For risk management to work effectively in the AA, the following are required:

- › An effective risk culture in place with risk management embedded in the business
- › The timely identification, reporting and management of the principal risks
- › The regular review and updating of risk registers, including the assessment of risks and their respective controls
- › Timely and accurate reporting of incidents and near misses
- › The operation of management "snap checks" (control effectiveness tests) to confirm the adequate operation of key controls
- › The implementation and tracking to resolution of management actions for risks outside of tolerance or appetite, deficient controls, incidents and issues

Risk Committee Report

continued

> The reporting of key risk indicators (KRIs)

> Engagement from all employees to effectively manage risk and operate the organisation's control framework

The effective operation of the above is monitored by the Committee. The AA's Risk Management Framework is reviewed annually by the Committee.

Group risk appetite

It is the responsibility of the Board to set and agree the Group risk appetite and this is regularly reviewed by the Committee. The appetite takes into account the level of risk and risk combinations that the Board is prepared to take to achieve the Company's strategic objectives together with the level of risk shock that the Group is able to withstand. The AA's Risk Appetite Framework outlines the amount of risk the organisation is willing to take.

Principal risks and uncertainties

The Board has identified, and monitors on an ongoing basis, the principal risks to the AA, including those risks that would threaten its strategy, future performance, solvency or liquidity. Set out on pages 34 to 37 are the risks the Board considers to be of most significance to the Group in terms of preventing or restricting execution of its strategy, together with the mitigating activities that we have put in place to try to prevent such risk materialising. We recognise that other risks are still present and seek to ensure that they are managed accordingly.

It is recognised that the Group is exposed to a number of risks, wider than those listed. However, we have disclosed those of most concern to the business at this moment in time, including those that have been the subject of debate at recent Board and Committee meetings.

Committee activity during the 2018 financial year

The Committee receives regular reports on risk management which include:

> The status of the principal risks and the top risks identified by executive management including horizon and emerging risks

> Material incidents and near misses

> Control effectiveness details

> Progress in completing actions to rectify control deficiencies

> The Group Risk Appetite Dashboard

> KRI exceptions

> Risk management Key Performance Indicators (KPIs)

> Minutes of the ERCC

> Updates from the chairs of the ARCCs

During the year, in addition to the standard reports from the Group Risk Manager and the Head of Compliance, the Committee has received presentations from various areas of the business to enable it to review and consider specific risks. Subjects covered have included:

> Information/cyber security (including the AA shop data breach and network access controls)

> Road Operations Service Levels

> Sales and Retention/Service – Quality Scores and Service Levels

> Preparations for implementation of the new GDPR requirements in 2018

> Complaint Handling

> Payment Cards – Secure Data Transfer and MasterCard & Visa Processing/preparation for the Revised Payment Services Directive (PSD2)

> IT and Business Transformation

> Updates on both the rectification of the dual/multiple cover issue for members and non members and customer renewal processes

> Cyber Insurance

Initiatives during the 2018 financial year

Initiatives to improve our Risk and Control Framework were noted in our Annual Report for the 2017 financial year – what we said we would do and what we have done:

Keep our Risk Framework and Culture fresh and relevant to the business, including simplifying the risk framework where possible, ensuring the risk management framework adds additional value to the business and provides a platform for employees to speak up and voice any concerns they may have

Actions undertaken:

> Risk reporting has been updated and improved

> The Group Risk team have continued to work with the business areas to make sure that new and changing risks are highlighted, and KRI exceptions reported

> The ERCC has been realigned and now has agenda items for "Significant Incidents, Near Misses and KRI triggers; Root Cause and Corrective Actions" and "Risk Deep Dives" together with the standard business area Risk Summaries

> A series of Speak Up roadshows facilitated by the Heads of Compliance and Internal Audit were run including training many staff in risk management and incident reporting

> The Whistle Blowing policy has been recommunicated with "Blow the whistle!" posters displayed at our premises

Use the Risk Management Framework to help support the ongoing cultural transformation in the AA

Actions undertaken:

- › Business Risk Forums have encouraged participants to speak up and share:
 - incidents and near misses including control failures and the root causes
 - changing and new risks
 - KPI/KRI exceptions
 - progress implementing corrective actions
- › Ongoing Risk Management framework training has been given to make sure the risk culture, framework and appetite is understood together with how the framework can be used to benefit the AA and protect stakeholders.

Improve the process for incident management to better learn from errors and ensure more timely effective resolution and the prevention of similar incidents

Actions undertaken:

- › The incident and near miss process has been refreshed
- › The Group Risk team has worked closely with the business to help rectify incidents and improve the control framework following identified issues.

Continued improvement to historic poor practices and processes

Actions undertaken:

- › The formation of the Central Assurance function has resulted in improved co-ordination, with Legal, Company Secretariat, Group Risk, Compliance, Data Protection/GDPR and business continuity planning
- › Internal Audit, Health & Safety, Corporate Insurance and Business Assurance are also included as attendees at the Central Assurance Steering Committee
- › The Group Risk team have worked with various business areas to help them process map key activities and better understand their processes and key controls

Improve the quality of the reporting that flows to the Committee

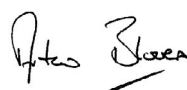
Actions undertaken:

- › As described above, the reporting to the Committee has been improved with greater focus on the key risks and material incidents and greater priority given to KRIs

The Committee's plan for the 2019 financial year includes:

We will:

- › Support the new Chief Risk Officer to improve risk culture through the business
- › Ensure Risk Appetite is better used in decision making
- › Integrate a revised Incident Management and root cause analysis process and procedures into normal business activity
- › Increase the Group Risk team's participation in Project Steering groups to include more of the Group's Top 50 projects. This will provide increased visibility on the identification and management of project risks
- › Refresh the process for the identification and reporting of Horizon/ Emerging risks
- › Review how best to measure and report risk culture in the organisation
- › Refresh the Snap Checks in place in the business to make sure they reflect changing working practices, evolving risks and the controls we place reliance on, to make sure the quality of the checking undertaken is satisfactory
- › Refresh the KRI MI suite to make sure that the KRIs are tracking the appropriate key risks and controls
- › Focus on the timely completion of actions arising from incidents and reviews



Andrew Blowers
Chair of the Risk Committee

Effectiveness

Audit Committee Report



The Committee has played a key oversight role in major decisions and initiatives within the business, acting to ensure the pace of change is appropriate.

Andrew Miller
Chair of the Audit Committee



Dear Shareholder,

I am pleased to present the report of the Audit Committee (the Committee) for the financial year ended 31 January 2018, during which the Committee has continued to review the Group's internal controls, consider significant financial reporting issues and judgements, and scrutinise the financial results prior to their submission to the Board.

As advised in the 2017 Annual Report the Committee undertook an audit tender process which resulted in the appointment of PwC with effect from the 2019 financial year. Further details on this matter are provided later in this report. The Committee also considered the ongoing relationship with Ernst & Young LLP in terms of the quality of their work and concluded that the effectiveness of the external audit process remained strong.

The Committee has continued to develop the themes addressed in the 2017 financial year, arising from the Financial Reporting Council's guidance on audit committees which takes full effect from this reporting year. These themes have been designed to ensure that the Committee's relationships with the Board, executive management, and internal and external auditors are characterised by a frank, open working relationship and a high level of mutual respect and that the Committee performs a role of oversight, assessment and review.

During the year the business has remained focused on the development of culture initiatives which included rolling out a staff engagement survey in December 2017. The results of the survey together with a schedule of actions to be undertaken during the next year as a result of the findings are presented in the Our people section on pages 40 to 42.

The dismissal of Bob Mackenzie and the appointment of John Leach as Chairman and Simon Breakwell as CEO have led to extensive changes in the leadership structure, which has further highlighted the focus on strategy.

The IT transformation project continued to be a focus as well as progress towards implementation of systems, processes and controls to seek compliance with the GDPR, which come into effect in May 2018.

The Committee has played a key role in these matters, taking a keen interest in the progress of initiatives, providing oversight and supervision while seeking to ensure the pace of change is appropriate.

The Committee comprises three members. With the exception of John Leach, who is now Chairman and will step down when an appropriate replacement is appointed to the Committee, all the other members are independent NEDs, who satisfy the requirements of the Code and the Committee's Terms of Reference.

As Chair of the Committee, I invite the CEO and the CFO to attend meetings of the Committee where appropriate and the Company Secretary attends as Committee Secretary. The Head of Internal Audit also attends regularly, except where the performance of internal audit is discussed. Jonathan Roe, as Chair of the ARCC of our regulated Insurance broker, AAISL, also regularly attends to ensure consistency and facilitate good communication across the Group. Other senior executives may attend as required to provide information on matters being discussed which fall into their area of responsibility. The Committee considers that receiving these updates helps to provide an insight into the business's challenges and aspirations as well as providing an opportunity to challenge and discuss these, while sharing our extensive experience and considering the issues with an independent perspective.

The external auditors, Ernst & Young LLP, also attend each meeting, except where discussion includes matters relating to their independence, performance and reappointment, fees or audit tendering.

Committee roles and responsibilities

The Committee members have an appropriately wide range and depth of relevant financial and commercial experience. These skills ensure that the Committee has the necessary range of competencies to fulfil its Terms of Reference, to provide an independent perspective, and to support effective governance. Furthermore, all three members of the Committee have recent and relevant financial experience. I am a member of the Institute of Chartered Accountants of Scotland and have recent experience as CFO of Trader Media Group, which owns Autotrader. John Leach is a Fellow of the Institute of Chartered Accountants and the Association of Corporate Treasurers. Andrew Blowers has extensive financial services experience (with a particular focus on the insurance industry) and has worked in an advisory capacity with the Financial Ombudsman Service. The Board therefore considers that the Committee meets the Code requirements in regards to its expertise.

All three members of this Committee sit on the Risk Committee and I, as Committee Chair, also sit on the Remuneration Committee, to facilitate efficient cross-communication and ensure that all risk and audit issues are addressed effectively.

The Committee meets regularly to fulfil the following core responsibilities:

- › Monitor the integrity and effectiveness of our financial reporting
- › Review and recommend the statutory, preliminary final and interim financial results to the Board
- › Maintain oversight of financial and other regulatory requirements and make recommendations as to the impact on our financial statements
- › Review and approve the internal audit plan for the following financial year, ensuring it is aligned with our key strategic priorities

The Committee ensures that regular updates are provided to the Board on how the Committee has discharged its responsibilities.

Full Terms of Reference of the Committee can be found at www.theaapl.com/investors/corporate-governance.aspx

Committee activity during the 2018 financial year

The Committee undertook the following activities during the year:

- › Oversaw a formal audit retender for the provision of external audit services
- › The Corporate Governance and Reporting Division of the Financial Reporting Council (FRC) conducted a thematic review of pension disclosures during the year. The AA plc Annual Report for the year ended 31 January 2017 was selected as part of this review. As a result of the review, the FRC identified the pension disclosures in the 2017 Annual Report as being an example of best practice
- › Oversaw progress towards delivery of the IT and business transformation programmes
- › Reviewed and made recommendations in relation to the statutory, preliminary final and interim financial results
- › Reviewed cash flows
- › Oversaw data protection and management of risk
- › Reviewed debt and financial instruments
- › Approved and oversaw key policies and practices
- › Reviewed the internal audit and compliance assurance plan, design and delivery, with particular focus on key strategic priorities
- › Assessed the effectiveness of the internal audit function and continued to keep under review the adequacy of internal controls
- › Reviewed and monitored the effectiveness, tenure and independence of the external auditor
- › Undertook a thorough review of the Annual Report and Accounts to ensure that the narrative messages are consistent and accurately reflect the financial statements and that the information as a whole is fair, balanced and understandable
- › Received reports from the AAISL Culture and Conduct Committee and the AAISL ARCC Chair
- › Reviewed progress of the GDPR compliance project

The Committee's action plan for the 2019 financial year

Looking ahead, the Committee will remain focused on the audit and assurance processes within the business, and maintain its oversight of financial and other regulatory requirements. The action plan for the 2019 financial year will focus on:

- › Ensuring a smooth transition to the new audit team at PwC
- › Ensuring a smooth transition to a new Audit Chair
- › Reviewing and making recommendations in relation to the statutory, preliminary final and interim financial results
- › Review of cash flow
- › Review of assurance plan, design and delivery, with particular focus on key strategic priorities
- › Approval of internal audit plan and oversight of key policies and practices
- › Assessing the effectiveness of the internal audit function and keeping under review the adequacy of internal controls
- › Undertaking a thorough review of the Annual Report and Accounts to ensure that the narrative messages are consistent and accurately reflect the financial statements and that the information as a whole is fair, balanced and understandable

Audit Committee Report

continued

Significant issues

The Committee has assessed whether suitable accounting policies have been adopted and whether management has made appropriate judgements and estimates.

Throughout the year, the finance team has worked closely with Ernst & Young LLP to ensure that the Group provides the required level of disclosure regarding the significant issues considered by the Committee in relation to the financial statements, as well as how these issues were addressed, while being mindful of matters that may be business sensitive.

The main areas of judgement that have been considered by the Committee to ensure that appropriate rigour has been applied are set out below.

The issue and its significance	Work undertaken	Outcome and actions
Revenue recognition	<p>The accounting policies for revenue recognition prepared by management have been presented to the Committee which has concluded that they remain consistent and appropriate. The Committee has reviewed management's assessment of the internal control framework over revenue which includes IT controls. This assessment has highlighted some issues with the initial revenue recognition of Roadside Assistance membership subscriptions by the membership database as well as the additional controls that management has put in place to identify and correct for these issues. The Committee notes that the current IT transformation plans include the replacement of the membership database which will improve the controls over revenue recognition in this area.</p> <p>Management has also carried out an impact assessment to determine the impact of adopting IFRS 15 "Revenue from contracts with customers" which is effective for the Group from 1 February 2018.</p>	<p>The Committee agrees with management's assessment that the internal controls have remained effective during the year, however there were instances where IT controls were not operating as documented and this will be subject to follow up work by the Committee.</p> <p>Based on the impact assessment of adopting IFRS 15, management has concluded that there will be no material impact on revenue from adopting this standard although additional disclosures will be required.</p>
Cyber security	<p>Review of existing administrative and technical controls in place to manage the risks associated with cyber security. This was based upon activity conducted by the Information Security team and included testing undertaken by an independent trusted security partner. This highlighted a number of areas of focus where remediation actions were needed to address known issues and vulnerabilities.</p>	<p>Work has been undertaken to implement and strengthen controls in this area, especially around access, licence management, use of PCs, laptops and databases. Oversight of this is now managed by the Risk Committee and in the coming year the Committee plans to review data in more detail.</p>
Pensions accounting	<p>The Group's defined benefit pension scheme is a significant net liability on the Group's balance sheet (see note 25 to the consolidated financial statements) and the value of the scheme will fluctuate due to changes in the underlying assumptions. The main assumptions which drive these fluctuations are forecast corporate bond yield rates and the forecast inflation rate.</p>	<p>The Committee has considered both the process that management undertook to finalise the assumptions and how these assumptions benchmark against the market. The Committee has concluded that the assumptions are consistent with the prior year and the overall valuation of the net liability is appropriately balanced.</p> <p>The Committee has also reviewed the disclosures relating to the defined benefit pension scheme and is satisfied that they are appropriate.</p>
Impairment of goodwill	<p>Management has prepared discounted cash flows based on the latest Board approved strategic plan. These discounted cash flows have been compared to the carrying value of goodwill. An impairment of goodwill of £26m has been identified in respect of the Driving Schools and £1m in respect of DriveTech.</p>	<p>The Committee has considered the basis of preparation of the discounted cash flows and is satisfied that these reflect the latest strategic plan of the Group. This identified that a historic goodwill balance allocated to driving schools was now impaired by £26m. In addition, a smaller impairment charge of £1m has also been incurred in the year as a result of impairment reviews carried out. See further details in note 26 to the consolidated financial statements. There is sufficient headroom compared to the carrying value of the remaining goodwill.</p>

External auditor

The Committee manages the relationship with the Group's external auditor on behalf of the Board.

Effectiveness, tenure and independence of the external auditor

Ernst & Young LLP has been the Group's auditor since the audit for the year ended 31 January 2008. The Company fully supports audit partner rotation and refreshment. Kathryn Barrow is the current audit partner, having been appointed during the 2016 financial year. The Committee considers annually the scope, fee, performance and independence of

the external auditor. After careful and thorough review, the Committee believes the independence and objectivity of the external auditor and the effectiveness of the audit process are safeguarded and remains strong. We have received confirmation from Ernst & Young LLP that they remained independent and objective within the context of applicable professional standards.

We have ensured that management confirmed compliance with our Group's policies on the employment of former Ernst & Young LLP employees and on the use of Ernst & Young LLP for non-audit work. The latter issue is discussed in further detail below.

Tender process for external audit services

During the 2017 financial year, in recognition of the FRC Ethical Standard 2016, the Committee approved the decision to commence a tender process for external audit services. The process took place during the 2018 financial year and concluded with the selection of PwC. This process meets the Code's requirement to put the external audit out to tender every ten years.

Three firms were invited to tender and as the current incumbent, Ernst & Young did not put themselves forward as a candidate for consideration. One firm declined to take part in the tender. The remaining two firms presented to a panel which consisted of myself as the Chair of the Committee, the CFO, Chair of the AAISL Audit, Risk and Culture Committee (ARCC), the Company Secretary, the Finance Director and the Chief Accountant. The AAISL ARCC Chairman and myself then met the lead partner of each firm together with the regulatory partner. An analysis of the firms was undertaken, which included a decision criteria scoring process. Conclusions were presented to the Committee for their discussion. Following consideration of the conclusions, the Committee recommended to the Board that PwC be appointed. The Board agreed with the recommendation and approved the appointment.

PwC will commence audit of the Group's financial statements with effect from the year ending 31 January 2019.

We would like to thank Ernst & Young LLP for their 11 years of service as auditors as well as, support for the IPO and three debt financings.

Audit fees

Details of fees paid to our auditors are listed in note 31. The audit fee for the 2018 financial year was £1m.

Non-audit fees

Project	2018 £'000	2017 £'000
July 2017 refinancing	86	–
AA Ireland disposal	–	201
FRS 101 conversion	–	20
December 2016 refinancing (final fee)	–	208
Total non-audit fees in financial year	86	429
<hr/>		
Audit fees	1,122	1,140
Non audit fee ratio	8%	38%

The Committee remains mindful of engaging the statutory auditor for non-audit services and of potential issues of independence and regularly reviewed the issue of non-audit fees at its meetings.

The Committee recognises that, in some instances, it is more timely and cost-effective for our audit firm, who are already familiar with the Group and its finances, to advise on non-audit matters. This is limited to work where the risk of the auditors' independence being impaired is low and where appropriate safeguards can be put in place. This has included in the year, work required by regulation in respect of the Group refinancing.

The Group has an external auditor independence policy (the Policy) in place which is reviewed annually by the Committee in light of relevant ethical guidance and the Committee seeks to ensure that it is adhered to.

The Group acknowledges and supports the FRC Revised Ethical Standards and our Policy reflects these revised standards and accordingly, sets out our commitment to maintaining a 70% cap on non-audit fees with the external auditor. The Committee will monitor compliance with the Policy as part of its role in reviewing auditor independence and the effectiveness of the audit process.

AA plc has complied throughout the 2018 financial year with the provisions of the Statutory Audit Services Order 2014 issued by the Competition and Markets Authority.

Internal controls

The Committee works closely with the Risk Committee and has completed its review of the Group's systems of internal controls and their effectiveness for the 2018 financial year and has done so in accordance with the requirements of the Code. It should be noted that the Group's risk management systems are designed to manage rather than eliminate the risk of failure to achieve business objectives and they can only provide reasonable and not absolute assurance against material misstatement or loss.

The review included, among other things, consideration of:

- > The Company's risk appetite (as described in the Risk Management section on pages 32-33)
- > The operation of the risk management and internal control system, including the output from an internal audit review of this area
- > The assessment of risks within the three-year business planning process
- > The principal risks facing the business, along with the changes to those risks during the year and the mitigating actions being taken in respect of them (see details in the Risk Management section on pages 34-37)
- > The outputs from the risk incident and near miss reporting process

In the Committee's opinion, there were no significant failings noted from this review however a number of recommendations were made, particularly in respect of the IT controls environment. The Group has adopted acceptable and appropriate accounting policies and made appropriate estimates and judgements as and where necessary. The Committee also believes that this Annual Report and Accounts provides the information necessary for shareholders to make an assessment as to the Group's performance, business model and ongoing strategy.

The Committee also works with the Risk Committee:

- > Ensures that there is an ongoing process for identifying, evaluating and managing the principal risks faced by the Company and the Group
- > Confirms that the systems have been in place for the year under review and up to the date of approval of the Annual Report and Accounts
- > Confirms that they are regularly reviewed by the Board
- > Ensures that the internal control systems accord with the FRC Guidance

Further details on our risk management can be found on pages 32-37 and in our Risk Committee Report on pages 67 to 69.

The Group's internal control and risk management systems ensure the accuracy and reliability of financial reporting. The key features of those systems include:

- > Documented financial governance framework
- > Comprehensive budgeting and reporting processes
- > Defined lines of accountability and delegation of authority
- > Review and approval of key accounting policies and estimates
- > Preparation of consolidated accounts
- > Investment appraisal process for evaluating major capital expenditure
- > An embedded whistleblowing policy
- > Project governance and information security

Audit Committee Report

continued

Committee review

As part of the external Board evaluation process carried out during the year by Condign, the Committee was considered to be working effectively. More details of the review can be found on page 58.

Fair, balanced and understandable

At the request of the Board, the Committee considered whether, in its opinion, the Annual Report and Accounts for the 2018 financial year is fair, balanced and understandable and whether it provides the information necessary for shareholders to assess the Group's performance, business model and strategy.

As part of this process, the Committee discussed what information and level of debate and insight it would need in order to satisfy members that financial information was fair, balanced and understandable.

The Committee was provided with a copy of the Annual Report early in the drafting process in order to assess the broad direction and key messages being communicated. The Committee received further drafts prior to the meeting at which it would be requested to provide its final opinion.

When forming its opinion, the Committee reflected on the information it had received and its discussions throughout the year. In particular, the Committee considered:

Is the report fair?

- > Is the whole story presented clearly and articulately?
- > Are the key messages in the narrative reflected in the financial reporting?
- > Has any sensitive material been omitted?
- > Are the KPIs disclosed at an appropriate level based on the financial reporting and how the business measures performance?
- > Is the reporting on the business segments in the narrative reporting consistent with that used for the financial reporting in the financial statements?

Is the report balanced?

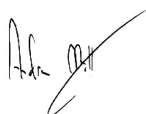
- > Is there consistency between the narrative reporting in the front and the financial reporting in the back of the report?
- > Do you get the same message when you read the two parts independently?
- > Are the statutory and adjusted measures explained clearly with appropriate priority and prominence?
- > Are the key judgements referred to in the narrative reporting and the significant issues reported in this Committee Report consistent with the disclosure of key estimation uncertainties and critical judgements set out in the financial statements? How do these compare with the risks that Ernst & Young LLP is planning on including in its report?

Is the report understandable?

- > Is there a clear and understandable structure and presentation to the report?
- > Is the language clear and the layout easy to navigate with good linkage throughout in a manner that reflects the whole story?
- > Are the important messages highlighted appropriately throughout the document?

Following its review, the Committee is of the opinion that this Annual Report and Accounts for the 2018 financial year is representative of the year, is consistent with its understanding of the business and results, and presents a fair, balanced and understandable overview, providing the necessary information for shareholders to assess the Group's performance, business model and strategy.

This will be my final report as Committee Chair as I will not be standing for re-election at the 2018 AGM. I wish the Company every success in the future.



Andrew Miller

Chair of the Audit Committee

Remuneration

Directors' Remuneration Report



This has been a challenging year, but we are now normalising the AA's remuneration structures to align more closely with good practice, in our drive to build a better AA.

Suzi Williams

Chair of the Remuneration Committee



Dear Shareholder,

On behalf of the Remuneration Committee (the Committee), I present the Directors' Remuneration Report in respect of 2018.

It has been a challenging year during which the Committee has been required to respond to some difficult circumstances. It has also been a period of renewal and of fresh starts, with a new CEO and a new strategy to build a better AA for our stakeholders. As a result, the Committee has been required to consider the executive pay structures which best align to this – in terms of both governance and shareholder value creation.

Departure of the Executive Chairman and appointment of Acting CEO

On 1 August 2017, the Board dismissed the former Executive Chairman. There was a need to make a swift interim appointment and Simon Breakwell agreed to take on the role of Acting CEO.

No payment for loss of office was made in connection with the former Executive Chairman's departure. Following his departure from the Company, the Committee resolved that the former Executive Chairman would forfeit all interests in the legacy MVP share arrangements.

The compensation for the Acting CEO was set at equivalent base salary and annual bonus opportunity as the previous Executive Chairman (pro-rated for the interim period) but with no participation in long term incentive schemes.

Appointment of CEO

During the search and selection process the Committee gave consideration to the remuneration package for the permanent CEO. The Committee's objective has always been to transition over time, towards more conventional, good practice UK listed company pay arrangements. Hence, when considering the package for an incoming CEO appointment, the Committee took the opportunity to better align our approach with mainstream FTSE remuneration practices. This would include:

- › No further awards under the highly leveraged MVP share arrangements.
- › Long term share incentives under a mainstream Performance Share Plan with annual awards in line with normal practice.
- › Good governance remuneration features such as malus, clawback and holding periods.

The Board was delighted to appoint Simon Breakwell to the role of CEO. In particular, his experience in running large operations coupled with his strong digital background, mean he is well-placed to drive our transformation and build a better AA with a better future.

On appointment, he was granted a long-term share award under the Performance Share Plan over 1.15m shares. The ongoing remuneration arrangements were set as follows:

- › Base salary at £700,000 - which is £50,000 lower than the previous Executive Chairman.
- › No participation in the MVP share awards.
- › Maximum annual bonus of 150% of salary – with mandatory share deferral.
- › PSP opportunity of up to 200% of salary per annum – awards subject to a two-year holding period.
- › Shareholding guidelines of 200% of salary – to be built up over five years.

Directors' Remuneration Report

continued

PSP performance measures and targets

Following his appointment, Simon undertook a rigorous review of the business and developed our new strategy, which was announced to our shareholders on 21 February 2018.

The next few years will be a critical time for the AA as Simon leads substantial change to modernise our business and deliver sustainable growth for our shareholders. Against that background, it is important that the measures and targets for our long term plan are aligned to our strategy. Following the announcement of the preliminary results for the year, the Committee will be consulting with major shareholders regarding measures and metrics for the long-term share awards granted under the PSP.

While the Committee had originally hoped to have completed this process prior to the publication of the Remuneration Report, we were also keen to ensure a robust process of engagement with shareholders so that their views could be represented in the Committee's final deliberations.

We remain committed to providing transparent disclosure of our approach to pay and therefore once the final terms have been agreed we intend to provide additional disclosure of the targets and awards, and are working towards this being on our website in advance of the AGM.

Annual bonus out-turns for the 2018 financial year

This has been a challenging year for the AA and of course this is reflected in our bonus out-turns.

The profit targets we set at the start of the year have not been met. In that context, whilst Martin Clarke delivered strongly against his individual objectives for the year, he has requested not to be considered for a bonus.

Simon Breakwell was appointed as Acting CEO midway through the year. The Committee therefore concluded that it was fair for his part-year bonus to be based on the profit guidance provided to the market at the time of mid-year results in September 2017. These profit targets were complemented with a set of key strategic priorities for the period leading to the year-end. The profit outcome was within the target range. He also achieved against his strategic priorities.

Simon Breakwell requested that his annual bonus outcome be reduced to reflect bonus outcomes for the wider AA team, and the Committee exercised discretion to reduce the outcome by 10%. Simon has decided to use the whole of his annual bonus to purchase AA shares.

Approval for new policy

This 2018 AGM will be the third anniversary of shareholder approval of our binding policy in 2015. Therefore, in accordance with the UK regulatory regime, shareholders will be provided with a binding vote in respect of our 2018 Policy.

For the purpose of the policy, the key changes are to reflect our new UK listed practice incentive policy (150% annual bonus and 200% PSP, rather than 120% annual bonus and participation in the leveraged MVP share arrangement) and the introduction of bonus deferral and holding periods.

Share ownership

The Committee has introduced a new shareholding requirement of 200% of salary. Simon Breakwell will build up this holding during the course of his tenure. As a step towards meeting this guideline, Simon has voluntarily decided to invest his full after-tax FY18 bonus into shares. Over a number of years, Martin Clarke has personally chosen to retain and build on his very significant shareholding in the Company, which means that he has been aligned with the experience of our shareholders since IPO.

In the wider organisation we have been pleased by the take-up of the all-employee share incentive plan (ESIP), which is now operated on an ongoing basis. There are currently 33.2% of employees participating in the plan and the Board is pleased to see employees across the business have shares in the Company.

Summary

As I outlined at the start, this has been a challenging year for the business and for our shareholders. Our approach to remuneration has sought to normalise the AA's remuneration structures, and deliver alignment with the shareholder experience, whilst at the same time supporting the appointment of new leadership and our drive to build a better AA.



Suzi Williams

Chair of the Remuneration Committee

ANNUAL REPORT ON REMUNERATION

This section of the Directors' Remuneration Report sets out a summary of how we intend to implement the 2018 Policy in the forthcoming financial year, as well as information on remuneration paid to Directors during the 2018 financial year. Where information has been audited, this has been stated. The Committee Chair's statement provides further context to the decisions made.

IMPLEMENTATION FOR THE 2019 FINANCIAL YEAR

A new Remuneration Policy will be presented to shareholders for approval at the 2018 AGM (2018 Policy). Subject to shareholder approval of this new Remuneration Policy, the following summarises how remuneration arrangements will be operated for the 2019 financial year.

SALARY AND BENEFITS

The annual salary levels of the Executive Directors are set out in the table below.

	FY19 salary
Simon Breakwell	£700,000
Martin Clarke	£480,000

The ongoing arrangements for Simon Breakwell, the CEO, took effect from 1 February 2018. The CEO's ongoing salary has been set at a level that is £50,000 lower than the previous Executive Chairman. The salary for Martin Clarke, the CFO, has not been increased since 1 February 2015.

Role appropriate benefits are provided to both Executive Directors. In line with the policy, Executive Directors receive a supplement of 11.7% of salary in lieu of participation in any Company pension plan.

ANNUAL BONUS

The maximum bonus opportunity for the CEO for the 2019 financial year will be 150% of salary. Up to 120% of salary would be payable in cash and up to 30% of salary would be deferred into shares for three years. The maximum bonus opportunity for the CFO will remain unchanged at 120% of salary.

For the 2019 financial year, the bonus will continue to be based on Trading EBITDA and strategic individual objectives, with the majority weighted towards Trading EBITDA.

The non-financial objectives are subject to a profit underpin. The precise performance targets for the coming year are considered to be commercially sensitive at present and the Committee provide expanded disclosure of targets on a retrospective basis.

The 2019 bonus will again be subject to both malus and clawback provisions.

LONG-TERM INCENTIVES

As part of the transition to more conventional incentive arrangements, long-term incentive awards are now granted under the Performance Share Plan (PSP). Under this plan, awards are subject to a three-year performance period and, for Executive Directors, a two-year holding period. PSP awards are also subject to malus and clawback provisions.

The Committee intends to set the performance criteria for this award so that there is close alignment to successful execution of the strategy and delivering for shareholders. The Committee will be consulting with major shareholders, following announcement of the preliminary results for the year, regarding the terms of this award including performance criteria. This process is still ongoing, and therefore the details of the proposed award have not been included in this report. Once the final terms have been determined, the Company intends to provide disclosure of the targets on our website prior to the AGM.

In line with best practice, for future awards the expectation is that the Company will provide prospective disclosure of proposed PSP awards including performance criteria in the Remuneration Report.

SHAREHOLDING REQUIREMENT

Executive Directors are expected to build up a holding of 200% of salary. Simon Breakwell will be expected to build up this shareholding within a reasonable timeframe, typically within five years of appointment. As at the year-end Martin Clarke's holding in AA shares exceeded 250% of salary based on the closing share price on 31 January 2018 of 126p.

IMPLEMENTATION IN THE 2018 FINANCIAL YEAR

Single total figure of remuneration (audited) - Executive Directors

The table below set out the total remuneration for the Executive Directors for the year ended 31 January 2018.

	Simon Breakwell ¹		Martin Clarke		Bob Mackenzie ² (Former Director)	
	2018 £000	2017 £000	2018 £000	2017 £000	2018 £000	2017 £000
Salary	375	–	480	480	399	750
NED fees	48	95	–	–	–	–
Taxable benefits	2	–	24	24	26	17
Retirement benefits ³	29	–	56	56	44	88
Short term incentives	311	–	–	346	–	514
Long-term incentives ⁴	–	–	–	–	–	–
Total	765	95	560	906	469	1,369

1 The remuneration shown for Simon Breakwell relates to his position as CEO in the period from 1 August 2017 onwards and fees paid in respect of his previous NED role.

2 Bob Mackenzie was dismissed from his position as Executive Chairman on 1 August 2017. No remuneration payment or payment for loss of office was made in connection with his departure. A payment was made in lieu of 8 days accrued holiday (totalling £22,000) which has been included in salary above.

3 Simon Breakwell received a supplement for retirement benefits of 11.7% from the date of his appointment as permanent CEO.

4 No long-term incentives vested in respect of the year. As at 31 January 2018 the only long-term incentive granted to Martin Clarke was in the form of MVP shares. The first test of the performance conditions for MVP shares was undertaken on the third anniversary of Admission, in June 2017, and performance conditions were not met at that time.

Directors' Remuneration Report

continued

Additional notes to the table

Remuneration arrangements for Simon Breakwell

Simon Breakwell was initially appointed as interim CEO on 1 August 2017, following Bob Mackenzie's dismissal. At the time of this appointment it was agreed that Simon's interim annual salary would be set at £750,000 and he would be entitled to a maximum bonus of up to 120% of salary (pro-rated for time in post). This interim salary and bonus was the same as for the previous Executive Chairman, however, with no participation in the MVP arrangements. These terms remained in place for the 2018 financial year.

Following the completion of the search and selection process for the Chief Executive role, Simon Breakwell was appointed as CEO on 25 September 2017. The Committee carefully considered the remuneration package, taking into account the size and complexity of the organisation, the scale of the transformation and the Committee's desire to move to more conventional FTSE remuneration practices.

In this context, the Committee determined that:

- › The base salary for the CEO will be £700,000, which is £50,000 lower than the previous Executive Chairman.
- › The CEO would not participate in the MVP share arrangement which was put in place for the Executive Directors prior to Admission.
- › The maximum bonus opportunity for the CEO will (subject to approval of the 2018 Policy) be 150% of salary, of which a portion will be deferred into shares.
- › Long-term incentives will be in the form of conventional performance share awards granted under the Performance Share Plan (PSP). These awards will be subject to a two-year holding period.

On appointment, Simon Breakwell was granted a long-term share award under the Performance Share Plan. Further details of this award are set out on page 79 below.

Taxable benefits

The benefits for the Executive Directors include a car related benefit, private medical insurance, permanent health insurance and life assurance. Life cover is four times annual salary payable should death in service occur. Private medical insurance is provided for the Executive only (family cover at the additional cost to the Executive Director). Permanent health insurance cover equal to 75% of the Executive Director's annual salary is provided (as long as the Executive Director is a member of the AA UK pension scheme, or otherwise by arrangement).

Retirement benefits

The amount set out in the table represents the Company contribution to the Executive Directors' retirement planning. The Company makes contributions equal to 11.7% of annual basic salary. Simon Breakwell was entitled to this contribution from the date of his permanent appointment to the role.

Short term incentives – annual bonus

As described above, Simon Breakwell was initially appointed as Chief Executive on an interim basis in August 2017. The 120% bonus opportunity was pro-rated to reflect the time in post and was therefore capped at 60% of his annual interim salary for the year. Consistent with best practice awards were subject to malus and clawback provisions.

Given that performance was to be assessed over a shortened period, the Committee concluded that the structure of the bonus should be tailored with the majority of the award linked to delivery of key short-term strategic priorities.

For FY18, 40% of his award was linked to Trading EBITDA, with targets built around the profit guidance provided to the market at the time of mid-year results. Performance against the Trading EBITDA targets was as follows:

Performance measure	Performance achieved	20% of element	60% of element	100% of element	Outcome (% of element)
Trading EBITDA	£391m	£372.9m	£392.5m	£412.1m	57%

The balance of the award (60%) was based on a scorecard of strategic priorities identified by the Board. The strategic element was based on objectives relating to people, the IT transformation and development of the new strategy. Key performance highlights from the strategic targets are summarised in the table below:

Performance measure	Performance achieved	Outcome
People	<ul style="list-style-type: none"> › Objectives related to reviewing the organisational structure › A full review of senior talent was undertaken, key internal talent was identified and fresh talent has been brought into the senior management team › Completion of first employee engagement survey for several years, completed by 78% of our employees › Retain focus of highly engaged and committed workforce 	16/20
IT transformation	<ul style="list-style-type: none"> › A full tech and data audit was initiated to fully understand the capabilities of the business › Review of breakdown and membership IT systems and change to implementation approach during the year › Long-term action plan developed and approved 	19/20
Strategy	<ul style="list-style-type: none"> › Detailed review of business, and development of new strategy for Building a Better AA, with clear targets and objectives › Launch of strategy to market in February 2018 	18.5/20

Based on the above performance outcomes, the CEO accrued a bonus equivalent to 76% of the maximum. Simon Breakwell recommended that his bonus outcome should be capped to be aligned with outcomes for the wider management team. The Committee exercised discretion to scale back the FY18 bonus by 10%. This resulted in a bonus of 69% of maximum (41% of his annual interim salary).

Simon Breakwell has voluntarily elected to use 100% of his after-tax FY18 bonus to purchase AA shares, after announcement of the preliminary results, in order to increase alignment with the future performance of the business and the longer-term shareholder experience.

For Martin Clarke, the 2018 bonus was subject to a maximum of 120% of salary and was subject to Trading EBITDA performance (70% of the overall bonus), and individual objectives (30%). The threshold Trading EBITDA target of £400m was not met.

Martin Clarke delivered strong performance against his individual objectives. Key performance highlights are summarised in the table below:

Performance measure	Performance achieved
Individual objectives	<p>› Successful refinancing which further reduced the cost of borrowings and extended the average maturity of our debt. Since the IPO in June 2014 annual debt interest costs has been reduced by £90m excluding the hedging costs</p> <p>› Conclusion of the triennial review of the AA's UK defined benefit pension scheme and agreed a funding plan for the deficit. Overall, the changes have reduced our exposure to pension risks, increased our competitiveness within our industry, and provided for a more consistent pension offering across our business</p> <p>› Key role in budgeting process in development of the forward looking strategy</p> <p>› Work relating to reorganisation of the finance function</p> <p>› Ensuring continued compliance for regulated businesses</p>

Martin Clarke informed the Committee that he did not wish to be considered for a bonus in respect of FY18.

In respect of the FY17 bonus, the Company agreed to disclose further detail regarding the financial targets on a retrospective basis in this year's report. As disclosed in last year's report, 38% out of 70% of the maximum bonus was earned based on the FY17 Trading EBITDA result of £403m. For the FY17 bonus, 20% of this element was payable for Trading EBITDA of £386m, 60% was payable for £406m and 100% was payable for £427m.

Legacy scheme: MVP shares

No long-term incentive awards vested during the year.

The MVP shares structure was implemented at Admission in order to align the interests of the MBI team and management with those of shareholders in the period following Admission. Martin Clarke retains an interest in MVP shares. Simon Breakwell does not hold any MVP shares and will not participate in this arrangement.

Awards were granted in the form of A, B and C shares that would convert into ordinary shares of the Company provided a TSR hurdle of 12% per annum was achieved over the three to five year period following Admission.

The first review of the A share performance hurdle was undertaken in June 2017. The TSR performance condition was not met in June 2017 and therefore the first tranche of this award did not convert into ordinary shares of the Company. The next review of performance against the hurdle will be undertaken in June 2018. It is not currently expected that the performance hurdle will be met.

There is one further testing date in June 2019. If no vesting occurs on that date, the MVP shares become cancellable for a total of £0.01.

Performance Share Plan

On appointment as CEO, Simon Breakwell was granted an award under the terms of the PSP. Although no buy-out award was made on appointment, the Committee did take into account reward opportunities forfeited by Simon Breakwell as a result of his appointment. The award level remained within the limit of the recruitment policy approved by shareholders.

As noted above, the Committee will be consulting with major shareholders regarding the performance criteria for this award. This process is still ongoing, and therefore the final targets have not been included in this report. Once the final targets have been determined, the Company intends to provide disclosure of the targets on our website prior to the 2018 AGM.

While the 2015 Remuneration Policy did not envisage a holding period, the Committee has determined that it would be appropriate for the 2017 award to be subject to an additional holding period after the end of the performance period. It is intended that a holding period will apply to this award, so that 50% of any vested shares will be released on the 4th anniversary of the grant date, with the balance released on the 5th anniversary of the grant date.

Scheme interests awarded during the financial year

	Grant date	Number of shares	Percentage vesting at threshold performance	Performance period	Vesting period
Simon Breakwell	27 October 2017	1,148,606 ¹	25% of FY18 to FY20 maximum	FY18 to FY20	3 years

¹ Based on the 10-day average share price prior to the date of grant (161.5p), the face value of the award is £1,855,000. This was equivalent to 247% of Simon Breakwell's annual interim salary for FY18 or 265% of Simon Breakwell's FY19 salary.

No PSP awards were granted to Martin Clarke in FY18, and he had no outstanding awards under this plan as at the year end.

Payment for loss of office and payments to former directors

Bob Mackenzie was dismissed as Executive Chairman of the Company on 1 August 2017. Bob Mackenzie received payment of salary and benefits whilst a Director only. A payment in lieu of eight days accrued holiday (totalling £22,000) was made but no other payment has been made in connection with his departure. Following his departure from the Company, the Committee resolved that Bob Mackenzie will forfeit all interests in the legacy MVP share arrangement in accordance with the provisions of the Articles of the Association.

During the year no other payments were made to past directors.

NON-EXECUTIVE DIRECTORS

Single total figure of remuneration (audited) – Non-Executive Directors

The table below sets out the total remuneration for Non-Executive Directors for the year ended 31 January 2018.

Name (role)	2018			2017		
	Fees £'000	Benefits £'000	Total £'000	Fees £'000	Benefits £'000	Total £'000
John Leach ¹	223	–	223	170	–	170
Andrew Blowers ²	129	–	129	115	–	115
Simon Breakwell ³	48	–	48	95	–	95
Andrew Miller	95	–	95	95	–	95
Suzi Williams ⁴	87	–	87	80	–	80

¹ John Leach was SID until 31 July 2017 on £170,000 per annum and was appointed Non-Executive Chairman on £275,000 from 1 August 2017.

² Andrew Blowers is Chairman of the Group's Insurer and is paid an additional fee of £27,500 per annum (2017: £20,000) for that role. Andrew was appointed as SID on 1 August 2017 at which point his total fees increased from £115,000 per annum to £135,000.

³ The figures shown in this table relate to the period to 31 July 2017 when Simon Breakwell served as a Non-Executive Director. Details of remuneration as CEO for the period from 1 August 2017 are set out on page 77.

⁴ Suzi Williams was appointed Chair of the Remuneration Committee on 1 August 2017.

Directors' Remuneration Report

continued

The current fees payable to the Non-Executive Directors are shown in the following table.

Role	FY18 fee	FY17 fee
Non-Executive Chairman ¹	£275,000	N/A
Senior Independent Director (SID) ²	£12,500	£170,000 ²
Basic fee for other Non-Executive Directors	£80,000	£80,000
Additional fee for chairing of Board Committee (other than Nomination Committee)	£15,000	£15,000
Additional fee for chairing of Group Insurer Board ³	£27,500	£20,000

1 John Leach assumed the role of Non-Executive Chairman with effect from 1 August 2017.

2 Under the previous Board structure the Chairman held an executive role, and therefore the SID had an expanded role as the most senior independent Director on the Board. Following the Board changes which took effect from 1 August 2017, the Chairman is now a non-executive role and therefore this is reflected in the FY18 SID fee.

3 The fee for chairing the Group Insurer Board increased on 1 February 2017.

Statement of Directors' shareholding and share interests (audited)

The Committee is supportive of Executive Directors building up and maintaining a significant holding in the Company.

During the course of his tenure, Simon Breakwell is expected to build a shareholding towards the guideline of 200% of salary. As noted above, Simon Breakwell intends to use his after-tax FY18 bonus in order to purchase shares in the Company. As at the year end, Martin Clarke has built up a shareholding in excess of 250% of his salary (based on the closing share price on 31 January 2018 of 126p). The Committee views these holdings as a key means of aligning their interests with those of shareholders. The table below sets out the Directors' (and any relevant connected persons) share interests in the ordinary shares of the Company as at 31 January 2018.

	Shares held outright (a)	Held in ESIP trust (b)	Deferred shares (c)	PSP – awards subject to performance conditions (d)	Shareholding (% of salary) (e)
Executive Directors					
Simon Breakwell ^(f)	–	–	–	1,148,606	n/a
Martin Clarke	1,087,500	2,462	2,213	n/a	285
Non-Executive Directors					
John Leach	32,812	–	–	–	n/a
Andrew Blowers	9,160	–	–	–	n/a
Andrew Miller	–	–	–	–	n/a
Suzi Williams	–	–	–	–	n/a
Former Directors					
Bob Mackenzie ^(g)	875,000	1,825	–	–	n/a

(a) Ordinary dividends were received on the shares held outright during the year.

(b) Includes partnership and dividend shares under the all-employee ESIP.

(c) Includes unvested matching shares under the ESIP.

(d) Award granted in October 2017 under the 2015 Performance Share Plan.

(e) Based on the closing share price on 31 January 2018 of 126p.

(f) Simon Breakwell sought approval to buy ordinary shares following his permanent appointment as CEO. However, dealings were restricted by Closed Periods which will end with the announcement of preliminary results on 17 April 2018.

(g) The data shown for Bob Mackenzie represents his interest as at 1 August 2017, when he ceased to be an Executive Director.

Martin Clarke received an additional interest of 467 partnership shares and 467 unvested matching shares under the ESIP scheme between 31 January 2018 and 16 April 2018, the latter being the latest practicable date prior to publication of this Annual Report.

There has otherwise been no change to the interests reported between 31 January 2018 and 16 April 2018.

The table below sets out the interests in MVP shares from current and former Directors as at the year-end.

Name	MVP shares		
	Subscribed prior to Admission	Subscribed in December 2015	Total
Executive Directors			
Martin Clarke	8.8%	13.2%	22.0%
Bob Mackenzie ¹ (former director)	22.4%	32.6%	55.0%
Nick Hewitt (former director)	8.8%	–	8.8%
Total	40.0%	45.8%	85.8%

1 On 16 April 2018 the MVP shares held by Bob Mackenzie were compulsorily transferred to the Company's EBT.

Simon Breakwell and the Non-Executive Directors do not have any interests in MVP shares. The remaining 14.2% of MVP shares were issued to the Company's Employee Benefit Trust for the benefit of senior management below Board level. The 55% of shares held by Bob Mackenzie at the year-end were acquired by the EBT for £0.01 on 16 April 2018.

The final value of MVP shares will be dependent on the level of TSR generated. The total value of all the A, B and C shares will be calculated as follows:

Annualised TSR	Value of MVP shares
Below 12%	nil
At or above 12%	5% of the TSR generated up to the 12% hurdle and 10% of the TSR generated over and above the 12% hurdle

During the year it has come to the Remuneration Committee's attention that there was a drafting omission in the Articles of Association with respect to the performance criteria for MVP shares which resulted in the risk that value could accrue to the MVP shares in certain scenarios where TSR growth was less than 12% per annum. As this was not consistent with the original intention, the Company will be seeking an amendment to the terms of the MVP shares contained in the Articles of Association, to ensure that value only accrues where growth exceeds 12% per annum. This change will require the approval of both shareholders and class holders (i.e. MVP share participants) and the Company proposes to put a special resolution to shareholders at the AGM scheduled for 7 June 2018, and separately in advance to classholders to implement this amendment. As a holder of MVP shares, Martin Clarke has already provided undertakings to confirm his agreement to this change to the terms of his MVP shares. The Committee has noted that based on the share price at the year-end, the MVP shares were significantly below the required threshold for vesting.

Service contracts and letters of appointment

Each of the Board Members will be proposed for re-election at the 2018 Annual General Meeting with the exception of Andrew Miller who will be standing down. The Executive Directors are employed under rolling service contracts that do not have fixed terms of appointment, but are normally subject to a 12-month notice period. Under the term of his appointment, Simon Breakwell has an initial notice period of 18 months which reduced down to 12-months with effect from 25 March 2018.

The Non-Executive Directors are appointed under a letter of appointment for an initial term of three years (subject to annual re-election at the AGM) which may be terminated by either party subject to a one-month notice period other than certain conditions under which the Company can terminate with immediate effect. The details of the Non-Executive Directors current terms are set out below:

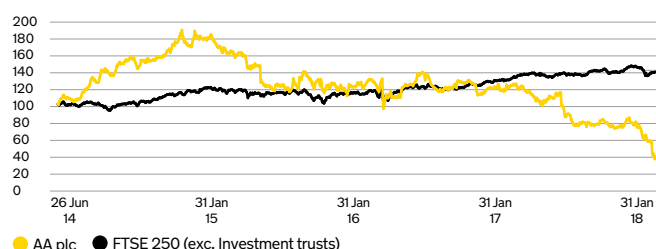
Name	Date of appointment	Term expires
John Leach	26 June 2014	9 June 2018 ¹
Andrew Blowers	25 September 2014	9 June 2018 ¹
Andrew Miller	26 June 2014	9 June 2018
Cathryn Riley	1 March 2018	9 June 2021
Suzi Williams	1 October 2015	1 October 2018 ¹

¹ It is the Company's intention that these expiry dates will be extended as the Board recommends election of Cathryn Riley and re-election of John Leach, Andrew Blowers and Suzi Williams at the AGM in accordance with the UK Corporate Governance Code. Andrew Miller will retire at the AGM and therefore his contract will expire on 7 June 2018.

Performance graph and table

The chart below illustrates AA Group's TSR performance against the FTSE 250 (excluding investment trusts) since Admission. This provides a general market reference point.

Value of £100 holding since admission



Source: Thomson Reuters Datastream

The table below shows the total remuneration paid to the CEO and/or Executive Chairman (as relevant) in each year since Admission.

		2015	2016	2017	2018 ¹
CEO single figure of remuneration	Simon Breakwell:	–	–	–	£765k
	Bob Mackenzie:	£1,113k	£1,557k	£1,369k	£469k
Annual bonus payout (% of maximum)	Simon Breakwell:	–	–	–	69%
	Bob Mackenzie:	100%	79%	57%	NIL
Long-term incentives vesting (% of maximum)	Simon Breakwell:	–	–	–	n/a
	Bob Mackenzie:	n/a	n/a	n/a	NIL

¹ The figures shown for each individual in FY18 reflect part-year figures.

Percentage change in remuneration of Director undertaking the role of CEO, Simon Breakwell

The table below illustrates the percentage change in salary, benefits and annual bonus for the 2018 financial year for the CEO as against all other employees.

	% change in base salary	% change in benefits ²	% change in annual bonus
CEO ¹	0%	n/a	21%
All employees ³	2%	0%	43%

¹ For the purpose of the year-on-year comparison, the annualised values for the CEO for FY18, have been compared to the FY17 values for the previous Executive Chairman.

² No changes to benefits provided.

³ Change in base salary for employees represents the average increase implemented as part of the Company's annual pay review in April 2017. The change in annual bonus represents the average bonus paid to employees.

The Remuneration Committee is mindful of pay conditions in the wider group, and take into account wider pay trends when determining remuneration for executive directors. The Remuneration Committee will play close attention to additional reporting regulations published in the coming months, including any requirements in relation to the disclosure of pay ratios. As the Government's preferred methodology for calculation of pay ratios has not yet been published, advanced disclosure of a pay ratio has not been provided in this year's report. However the Company expects to comply in full with any new requirements which come into effect in due course.

Relative importance of spend on pay

The table below illustrates the year-on-year change in the total remuneration costs for all employees against the Company's key performance metric of Trading EBITDA.

	2018 £m	2017 £m	% change
Total employee remuneration ¹	311	317	(0.6)
Trading EBITDA ²	391	403	(3.0)
Distributions relating to the year ³	30	57	(47.4)

¹ Excludes pension past service credit of £34m. (See note 8).

² Excludes results of discontinued operations.

³ The total cost of ordinary dividends declared to shareholders relating to the year.

Role of the Remuneration Committee

The Remuneration Committee is responsible for reviewing and making recommendations to the Board regarding the Remuneration Policy of the Group and for reviewing compliance with the policy. The CEO (and previously the Executive Chairman) and the Human Resources Director attended parts of Committee meetings by invitation in order to provide the Committee with additional context. The Company Secretary acts as the Committee's secretary. No individual was present when their own remuneration was being determined.

Deloitte LLP is engaged by the Committee as their advisers. Deloitte LLP received fees of £76,975 (2017: £36,750) for advice to the Committee on a time and materials basis. During the year, Deloitte LLP also provided the Company with HR consulting services and taxation advice. Deloitte LLP is one of the founding members of the Remuneration Consultants' Group and adheres to the Remuneration Consultants' Group's Code of Conduct. The Committee is satisfied that the advice it has received has been objective and independent.

The table below sets out the votes on the Annual Report on Remuneration at the 2017 AGM and the Remuneration Policy at the 2015 AGM.

	Votes for	Votes against	Votes abstained
Remuneration Report (2017 AGM)	93.1% (416.2m)	6.9% (30.7m)	1.7m
Remuneration Policy (2015 AGM)	94.8% (474.7m)	5.2% (26.3m)	42.3m

Directors' Remuneration Report

continued

Directors' Remuneration Policy

The following sections set out our Directors' Remuneration Policy (the 2018 Policy). This 2018 Policy will be presented to shareholders for approval at the 2018 Annual General Meeting, and will take immediate effect once approved.

Changes compared to the policy approved at the 2015 AGM

As noted in the statement from the Chair of the Remuneration Committee, the intention is for future remuneration arrangements to be more aligned with mainstream FTSE practices. This objective guided the content of the 2015 Policy Report, and has been maintained in respect of the updated policy.

Many of the key features of the 2015 policy have been retained. As part of the transition towards more mainstream pay practices, the Company

does not intend to make any further awards under the highly leveraged MVP share arrangement that was adopted pre-IPO. As noted in the Directors' Remuneration Report, Simon Breakwell's ongoing salary as CEO for FY19 has been set at a lower level than the previous Executive Chairman and he will not take part in the MVP share arrangement. Instead Simon Breakwell will receive a bonus opportunity of 150% of salary, which will be partially deferred into shares, and long-term incentive awards will be granted under the Performance Share Plan. The 2018 Policy reflects this change to the annual bonus.

The 2018 Policy has also been updated to align with evolving market and best practice and this includes the addition of a two-year holding period in respect of future awards under the Performance Share Plan, certain minor amendments have also been made to the detail of the 2018 Policy to aid implementation (e.g. additional detail on the malus and clawback terms).

Base salary

Purpose and link to strategy

To attract, retain and motivate executives of the calibre required to deliver the Group's strategy.

Operation

When reviewing salary levels the Committee takes into account a range of factors including:

- › The individual's skills, experience and performance
- › The size and scope of the individual's responsibilities
- › Market rate for the role
- › Pay and conditions elsewhere in the Group

Salary levels are typically reviewed annually by the Committee

Maximum opportunity

There is no overall maximum for salary opportunity or increases. Individual salaries are set based on the factors set out above.

The Executive Director salaries as at 1 February 2018 are:

- › Simon Breakwell: £700,000
- › Martin Clarke: £480,000

Performance metrics

None.

Benefits

Purpose and link to strategy

To provide competitive benefit arrangements appropriate for the role.

Operation

A range of benefits may be provided to Executive Directors including, but not limited to, car related benefits, life cover and private medical insurance.

From time to time the Committee may review the benefits provided for individual roles. Additional benefits may be provided where the Committee considers this appropriate (e.g. on relocation).

Executive Directors may also participate in any all-employee share plans (including the Company's Employee Share Incentive Plan) operated by the Company from time to time on the same terms as other employees.

Maximum opportunity

There is no overall maximum for benefits.

Participation in any HMRC-approved all-employee share plan is limited to the maximum award levels permitted by the relevant legislation.

Performance metrics

None.

Retirement benefits

Purpose and link to strategy

To provide a competitive level of retirement benefits appropriate for the role.

Operation

Executive Directors are eligible to participate in the AA UK pension scheme (or any other similar pension plan operated by the Group from time to time) or receive a cash allowance in lieu of participation.

For new hires the nature and value of any retirement benefit provided will be, in the Committee's opinion, reasonable in the context of market practice for comparable roles and take account of both the individual's circumstances and the cost to the Company.

Maximum opportunity

The maximum benefit is 25% of salary.

For the financial year commencing 1 February 2018 the personal pension or cash allowances for Executive Directors will be 11.7% of salary.

Performance metrics

None.

Annual bonus

Purpose and link to strategy

To incentivise the delivery of annual financial, strategic and operational objectives, which are selected to support our business strategy.

Operation

Performance metrics and targets are set annually to ensure they remain aligned with financial and strategic goals. Bonus levels are determined by the Committee after the year-end, based on an assessment of performance.

In order to facilitate share ownership, the Remuneration Committee may require a portion of any bonus earned to be deferred into shares over a period of three years (or such other period as the Committee may determine). The Remuneration Committee will be mindful of an Executive's shareholding when determining the level of deferral.

For FY2019, it is expected that 20% of Simon Breakwell's bonus will be deferred into shares.

Maximum opportunity

The maximum annual opportunity is 150% of salary.

For FY2019, the maximum opportunity for Simon Breakwell will be 150% of salary, and the maximum opportunity for Martin Clarke will be 120% of salary.

Performance metrics

Performance targets will be determined by the Committee at the beginning of each performance period, and may comprise of a combination of financial, strategic, operational and individual targets appropriate for the role.

At least 50% of the award will be subject to financial measures.

The threshold payout for the minimum level of performance will be determined by the Committee taking into account the nature of the target. There will normally be scaled payouts for performance between the minimum and maximum thresholds.

Recovery provisions

Malus and clawback provisions apply to all awards.

Scenarios in which these provision may be applied include material misstatement of the Company's financial statement, a material failure of risk management, the bonus outcome being determined on the basis of materially inaccurate information or serious misconduct by the participant.

Directors' Remuneration Report

continued

2015 Performance Share Plan

Purpose and link to strategy

To reward for the delivery of performance targets linked to long-term strategic objectives and to provide alignment with the interests of shareholders.

The Committee is, as planned, in the process of transitioning to an incentive structure which is more conventional for the UK listed environment. The Performance Share Plan (PSP) will provide the Committee with the facility to make annual long-term share awards subject to performance measures aligned to the success of the Company.

Operation

The PSP was approved by shareholders at the 2015 AGM.

Awards of conditional shares (or equivalent) will vest dependent on performance measured over a period of at least three years. Future awards will normally be subject to a two-year holding period following the end of the performance period.

The Committee will review the metrics, targets and weightings prior to grant to ensure they are aligned with the long-term strategic goals.

Dividends (or equivalents, including re-investment) may accrue in respect of any shares that vest.

Maximum opportunity

The maximum face value of awards in respect of any financial year is 200% of salary.

The level of payout for the threshold performance hurdle set would normally not exceed 25% of the maximum opportunity. Full vesting will require achievement of the stretch objectives set. There will normally be scaled vesting for performance between the threshold and maximum performance levels.

Performance condition

The Committee will determine the performance metrics, weightings and targets to ensure they are aligned with the corporate strategy.

The Committee would seek to engage appropriately with its major shareholders in relation to the performance conditions for initial awards and in respect of changes to criteria for subsequent awards to Executive Directors under this plan.

Recovery provisions

Malus and clawback provisions apply to all awards.

Scenarios in which these provision may be applied include material misstatement of the Company's financial statement, a material failure of risk management, the vesting outcome being determined on the basis of materially inaccurate information or serious misconduct by the participant.

Shareholding guidelines

Purpose and link to strategy

To aid alignment of Executive Directors with shareholders.

Operation

Executive Directors are expected to build up a holding of 200% of salary. Executive Directors will be expected to build up this shareholding within a reasonable timeframe, typically within five years of appointment.

Legacy arrangement – MVP shares on Admission

The Management Value Participation Shares (MVP shares) were implemented at Admission. The MVP shares are fully allocated and the Committee does not intend to allocate any further MVP shares.

Under the original terms, this legacy arrangement ceases in 2019. The CEO will not participate in this MVP share arrangement.

MVP shares

Purpose and link to strategy

To link reward with Company performance and long-term shareholder value creation following Admission. Awards are share-based to facilitate share ownership and further align the interests of participants and shareholders.

Operation

The MVP shares are a one-off structure implemented prior to Admission.

The MVP shares provide participation in the total shareholder return created over the first five years following Admission, provided a minimum hurdle rate is achieved.

The arrangement takes the form of A shares, B shares and C shares in the Company with each class representing a third of the total number of MVP shares. Unless the Committee determines otherwise, each participant will hold an equal number of A, B and C shares.

The A, B and C shares are convertible into ordinary shares in the Company or are redeemable following satisfaction of the relevant Performance Condition tested on the third, fourth and fifth anniversary of Admission respectively. The Performance Condition had not been met on the first review of the A share hurdle in June 2017. Therefore, the A shares did not convert into ordinary shares of the Company.

A further review of the A and B shares hurdle will be undertaken on the fourth anniversary of Admission on 26 June 2018. If the Performance Condition is not met on the fourth anniversary, but is satisfied on the fifth anniversary (including the requirement for further growth in TSR for that additional period), the A and B shares will be convertible or redeemable as described above. Value per share is based on the aggregate value calculated by reference to the performance conditions divided by the aggregate number of shares allocated.

In the event that the Performance Condition of any of the MVP shares has not been satisfied by the fifth anniversary of Admission, 26 June 2019, the Company will be able to acquire all of the MVP shares for £0.01 in aggregate from each shareholder. The same applies in the event that any holder has not required the Company to convert his MVP shares within the applicable timeframes.

Maximum opportunity

The maximum number of ordinary shares resulting from conversion of MVP shares will not in any 10 year period exceed 5% of the issued share capital (as calculated from time to time). 60 million MVP shares have been allocated under this structure.

The allocations of MVP shares were split into two tranches, 40% issued at Admission to the Executive Directors at that time and the remaining 60% allocated in 2016.

14.2% of the authorised MVP shares was approved by the Committee to be allocated to an Employee Benefit Trust for the benefit of other employees in the wider management team.

As at 31 January 2018, the allocations of MVP shares to current and former Executive Directors are as follows:

- > Martin Clarke: 22%
- > Nick Hewitt (former director): 8.8%
- > Bob Mackenzie (former director): 55%
- > Employment Benefit Trust: 14.2%

Following the dismissal of Bob Mackenzie the Board approved, under the compulsory transfer provisions in the Articles of Association, the transfer of his MVP shares to the Employee Benefit Trust.

Performance Condition

For all MVP shares, the Performance Condition is as set out in the Articles of Association and requires that the total shareholder return (TSR) per annum from Admission to the relevant measurement point is equal to or more than 12% (the Performance Condition).

If the Performance Condition is met, the value of the MVP shares shall be:

- > 5% of the TSR up to the Performance Condition; plus
- > 10% of the amount by which TSR exceeds the Performance Condition.

If the Performance Condition has been satisfied, the MVP shares may be converted into such number of ordinary shares at the average closing price of the share over the 10 business days prior to the relevant anniversary.

As noted in the Directors' Remuneration Report, a proposal will be put to shareholders at the 2018 AGM and to classholders for a correction to the Articles of Association to reflect the further 12% per annum TSR increase on any retesting.

Notes to the policy table – Further detailed provisions

The Committee may make any remuneration payments (including the vesting of incentives) and payments for loss of office notwithstanding that they are not in line with the 2018 Policy set out above, where the terms of that payment were agreed either: (i) before the 2015 Remuneration Policy came into effect; (ii) agreed during the term of, and consistent with, the 2015 Remuneration Policy; or (iii) at a time when the relevant individual was not a Director of the Company and, in the opinion of the Committee, the payment was not in contemplation of the individual becoming a Director of the Company.

All incentive awards including MVP shares and PSP awards are subject to the terms of the relevant Articles of Association or plan rules under which awards are allocated or granted. The Committee may adjust or amend awards or shares in accordance with the provisions of the Articles of Association, plan rules and relevant scheme documentation (as applicable). This includes making adjustments to awards to reflect corporate events, such as a change in the Company's capital structure.

The Committee may adjust the calibration of performance measures and vesting outcomes, or substitute or amend any vesting condition (e.g. due to a significant acquisition or disposal) provided that the resulting condition is appropriate and not materially less difficult to satisfy.

In the event of a change of control of the Company, which results from an offer to shareholders, if the price offered delivers a TSR for the period from Admission to the change of control in excess of the relevant performance condition then a holder of MVP shares has the right to require the Company to convert their MVP shares into such number of ordinary shares as represents the relevant proportion (based on the percentage of MVP shares as a proportion of the total number of MVP shares) of the aggregate value of the MVP shares. The Company (or, where the Company does not give notice to convert the shares by the given deadline, the holder of MVP shares) may elect to redeem, rather than convert the MVP shares. In the event of a winding up on or before the fifth anniversary of Admission, where the relevant performance condition is met, holders of MVP shares will be entitled to receive a cash amount reflecting their proportion of the aggregate value of the MVP shares. Vesting of any awards granted under the PSP will normally take account of the relevant performance condition and the time elapsed. Alternatively PSP awards may be rolled over into shares of the acquiring company.

The Committee may make minor amendments to the 2018 Policy to aid its operation or implementation without seeking shareholder approvals (e.g. for regulatory, exchange control, tax or administrative purposes).

Directors' Remuneration Report

continued

Performance measures and targets

The performance measures for the annual bonus are chosen to provide an appropriate incentive for Executive Directors to meet financial, strategic, operational and personal goals for the year. This approach allows the Remuneration Committee to effectively reward performance against the key elements of Group strategy. The bonus targets are set by the Remuneration Committee each year to ensure that Executive Directors are appropriately focused on the key objectives for the next 12 months. Targets are set by reference to the Company's business plan and budget.

The performance measures and targets for PSP awards will be aligned with the long-term strategic objectives of the Company and its shareholders. As noted in the statement from the Chair of the Remuneration Committee, the Company will consult with shareholders regarding the performance criteria for initial awards under the PSP after the announcement of the preliminary results.

Recruitment policy

The intention is that if any Executive Directors are appointed, they would be recruited under a conventional package comprising salary, benefits, annual bonus and PSP awards, with no participation in the legacy MVP shares.

Base salary would be set taking into account the principles set out in the policy table and may be set at a level higher or lower than the previous incumbent. A cash supplement may be paid for interim positions. Normally benefits will be consistent with benefits provided to existing Directors, however, additional benefits may be provided in certain circumstances (e.g. relocation allowance).

The Committee may, on appointing an Executive Director, need to 'buy out' remuneration arrangements forfeited on joining the Company. The form and value of any buyout would take into account the terms of the arrangements (e.g. form of award, performance conditions, timeframe) being forfeited. The overriding principle will be that any replacement buy-out awards will, in the opinion of the Committee, be no more valuable than the entitlement which has been forfeited.

The maximum level of variable pay would be determined taking into account the calibre of the candidate, the scale of the business and the nature of the strategic priorities at the time. For the purpose of this recruitment policy the maximum level of variable remuneration (i.e. short-term and long-term incentives) will not exceed 400% of salary per annum.

The Committee may determine that for the first year of appointment the annual bonus award will be subject to such conditions as it may consider appropriate.

Where an executive is appointed from within the Company, the normal policy of the Company is that any legacy arrangements would be honoured in line with their original terms and conditions. Similarly, if an Executive Director is appointed following the acquisition of or merger with another company, legacy terms and conditions would be honoured.

MVP shares are currently fully allocated and it is not intended that these would form part of the remuneration arrangements for a newly appointed Executive Director.

In the event of the appointment of a new Non-Executive Director or Chairman, remuneration arrangements will be in line with the principles detailed in the relevant table above.

Non-Executive Director fees

Approach to setting remuneration

Fees are set at appropriate levels to ensure Non-Executive Directors are paid to reflect the individual responsibility taken. Fees are reviewed periodically.

When setting fee levels, consideration is given to a number of internal and external factors including responsibilities and market positioning.

Benefits appropriate to the role may be provided. Travel and other reasonable expenses (including fees incurred in obtaining professional advice in the furtherance of their duties and any associated taxes) incurred in the course of performing their duties may be paid by the Company or reimbursed to Non-Executive Directors.

Opportunity

The total fees paid to Non-Executive Directors will remain within the limit stated in the Articles of Association.

Individual fees reflect responsibility, relevant experience and time commitment. Additional fees may be paid for further responsibilities, such as chairmanship of committees, duties related to subsidiary boards, or other periods of increased activity.

Service contracts and payments for loss of office

Notice period

The notice period for the current Executive Directors is 12 months. Service contracts for new Executive Directors will normally be limited to 12 months' notice. In limited circumstances the initial notice period for a new appointment may be longer than the Company's normal policy (up to a maximum of 18 months), with the notice period reducing down to 12 months over time.

Payments on cessation

The Company may terminate an Executive Director's service agreement at any time by making a payment in lieu of notice in respect of basic salary for the outstanding period of notice, together with accrued holiday entitlement.

Benefits (or a payment in lieu) may also be provided. This may include certain benefits in connection with termination, such as legal costs, outplacements costs and the costs of meeting any settlement agreement.

The Committee reserves the right to make any other payments in connection with a director's cessation of office or employment where the payments are made in good faith in discharge of an existing legal obligation (or by way of damages for breach of such an obligation) or by way of compromise or settlement of any claim arising in connection with the cessation of a director's office or employment.

The treatment of incentive awards in the event of cessation is determined by the relevant plan rules or the Articles of Association (in the case of the MVP shares) as summarised below.

Annual Bonus

In certain circumstances, an individual may receive a bonus for the period prior to cessation. The bonus amount may be pro-rated where departure occurs before the year-end.

Deferred shares relating to bonuses earned in prior years will generally be retained (other than in cases of gross misconduct), however they will remain subject to malus and clawback.

MVP shares

The treatment of MVP shares is set out in the Articles of Association.

In respect of MVP shares allocated prior to Admission, where an individual ceases employment by reason of bankruptcy, disqualification from acting as a director, conviction of a serious criminal offence, breach of any non-compete undertaking, any act of gross misconduct or act which brings the Group into disrepute, or any other reason justifying summary dismissal, or where the individual subsequently takes action or makes comments which denigrate the Group or bring the Group into disrepute, the Company may acquire the individual's shares for a nominal value of £0.01. In other circumstances, the individual will retain their interest.

In respect of subsequent MVP shares which are allocated, the Company will normally be able to acquire the individual's shares following cessation for a nominal value of £0.01, in the event that the individual is a bad leaver, and serve notice. To the extent permitted by the Articles of Association the Committee may determine that an individual is not a bad leaver. An individual will not be a bad leaver where cessation occurs as a result of death, permanent disability, redundancy, or the sale by the Group of the individual's employing business unit. An individual will be considered to be a bad leaver where he takes actions or makes comments which denigrate the Group or bring the Group into disrepute.

PSP

Under the plan rules, unvested awards will lapse on cessation of employment unless the participant is a good leaver.

Good leaver reasons include an individual ceasing employment by reason of death, ill-health, injury, disability, the sale of the business or entity that employs him out of the Group, or for any other reason at the Remuneration Committee's discretion.

Where an individual is considered by the Committee to be a good leaver, a participant's unvested award will usually continue until the normal vesting date (unless the Remuneration Committee determines that the Award should vest at an earlier date). In these circumstances awards will vest taking into account the extent to which any performance condition is satisfied and, unless the Remuneration Committee determines otherwise, the period of time that has elapsed from the date of grant.

Unless the Committee determines otherwise, where relevant, any holding period will continue to apply for at least 12 months following vesting.

All Non-Executive Directors are appointed in writing. The letters of appointment for the current Non-Executive Directors include a one month notice period (by either party) or no notice period if terminated by

shareholders. The Company may include a notice period for new appointments of no more than three months for Non-Executive Directors and no more than twelve months for a Non-Executive Chairman.

Directors' Remuneration Report

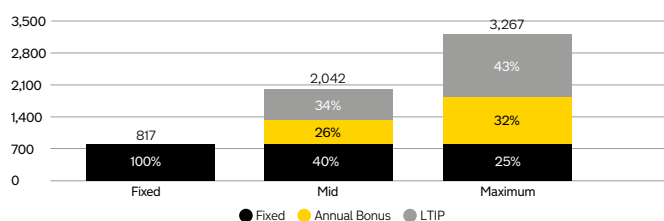
continued

Illustrations of application of remuneration policy

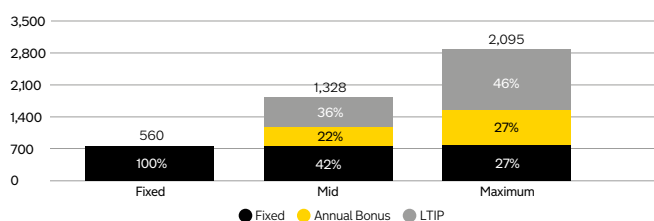
The following charts illustrate the different elements of the Executive Directors' remuneration under various different performance scenarios. The assumptions used are provided below the charts. In line with the

Regulations the illustrations exclude the impact of share price movement and dividends. The actual value of the annual bonus and PSP shares will vary depending on actual performance and may, therefore, differ from the illustrations set out below.

SIMON BREAKWELL (£000)



MARTIN CLARKE (£000)



		Minimum	Target	Maximum
Base salary for 2018/19				
Taxable benefits – assumed to be 5% of salary for illustration				
Retirement benefits – 11.7% of salary				
Fixed pay				
	Opportunity	Minimum	Target	Maximum
Annual bonus	CEO: 150% of salary CFO: 120% of salary	Nil	50% of maximum	100% of maximum
PSP	Based on the maximum award under the plan rules: 200% of salary	Nil	50% of maximum	100% of maximum

Remuneration in the wider employee group

The wider employee group participate in performance-based incentives. Throughout the Group, base salary and benefit levels are set taking into account prevailing market conditions. Differences between Executive Director pay policy and other employee pay reflect the seniority of the individuals, and the nature of responsibilities. The key difference in policy is that for Executive Directors a greater proportion of total remuneration is based on variable pay elements. The Committee has oversight of incentive plans operated throughout the Group. Below Board long-term incentives align with the long-term interests of the business and where appropriate objectives may be tailored to individual business areas.

When setting the policy for the remuneration of the Executive Directors, the Committee has regard to the pay and employment conditions of employees within the Group. The Committee reviews salary increases and pay conditions within the business, to provide context for decisions in respect of Executive Directors. However, the Committee does not use comparison metrics or consult directly with employees when formulating the 2018 Policy for Executive Directors.

Consideration of shareholder views

The Committee considers the views of its shareholders and is pleased to work towards best practice. The Company regularly engages with major shareholders to ensure that their views are considered when making key decisions relating to executive remuneration. As noted in the statement from the Chair of the Remuneration Committee, the Committee will consult with major shareholders regarding the operation of initial awards granted under the Performance Share Plan.

Directors' Report



This year for the AA has demonstrated the importance of a strong, independent Board and a good governance structure.

Mark Millar

General Counsel and Company Secretary



The Directors present their report together with the audited accounts for the year ended 31 January 2018.

This Directors' Report contains certain statutory, regulatory and other information. As permitted by the Companies Act 2006 (the Act), the following information which is required by law to be included in the Directors' Report is incorporated by reference:

- › Strategic report (pages 12 to 17)
- › Corporate governance report (pages 50 to 92)
- › Employee involvement and engagement (page 40)
- › Information about our people (pages 40 to 42)
- › Training and career development of disabled employees (page 41)
- › Carbon emissions (page 45)
- › Financial instruments (note 27)
- › Likely future developments (pages 12 to 17)
- › Related party transactions (note 32)
- › Events after the balance sheet date (note 36)

Company status

AA plc (the Company) is a public limited liability company with company number 5149111 and the holding company of the AA Group of companies (the AA). It holds a premium listing on the London Stock Exchange main market for listed securities.

Results and dividends

The results for the year ended 31 January 2018 are set out from pages 101 to 138. The Company paid an interim dividend of 3.6p per ordinary share on 10 November 2017 (2017: 3.6p). The Board has proposed a final dividend of 1.4p per ordinary share in respect of the year (2017: 5.7p) which, subject to approval by shareholders at the AGM to be held on 7 June 2018, will be payable on 12 June 2018 to shareholders on the register at the close of business on 4 May 2018, giving a total dividend in respect of the year of 5p per ordinary share (2017: 9.3p). The ex-dividend date will be 3 May 2018.

Share capital

The Company's issued share capital, as at 31 January 2018, comprised a single share class of ordinary shares which are listed on the London Stock Exchange and six classes of MVP shares. Details of the movements in the issued share capital can be found in note 23 of the financial statements. Each ordinary share carries the right to one vote at general meetings of the Company.

The issued and fully paid share capital of the Company as at 31 January 2018 is as follows:

Class	Nominal value	Number	Amount (£)	% Issued share capital
Ordinary	£0.001	610,807,568	610,808	100
MVP shares (A1 shares)	£0.001	8,000,000	8,000	40
MVP shares (B1 shares)	£0.001	8,000,000	8,000	40
MVP shares (C1 shares)	£0.001	8,000,000	8,000	40
MVP shares (A2 shares)	£0.001	12,000,000	12,000	60
MVP shares (B2 shares)	£0.001	12,000,000	12,000	60
MVP shares (C2 shares)	£0.001	12,000,000	12,000	60

The ordinary shares can be held in certificated or uncertificated form. Holders are entitled to attend and speak at general meetings of the Company, to appoint one or more proxies and, if they are corporations, corporate representatives are entitled to attend general meetings and to exercise voting rights. All issued ordinary shares are fully paid up.

Directors' Report

continued

The MVP shares are not listed on any public market and have no voting rights, except in respect of rights over the MVP shares. The Articles provide that holders of MVP or Deferred Shares must receive written consent from the Remuneration Committee before transferring their holding. The holders are entitled to receive ordinary shares or cash in the future, subject to satisfaction of performance conditions which require a minimum 12% compound total shareholder return performance condition over a three-to five-year period from Admission of the shares in June 2014. It is currently anticipated that the MVP shares will lapse at the end of June 2019. Further details of the MVP shares are set out on page 85.

Purchase of own shares

No ordinary shares were purchased by the Company during the 2018 financial year (2017: nil) nor to the date of this Annual Report. The existing authority granted to the Directors to make market purchases of its ordinary shares expires at the end of the AGM to be held on 7 June 2018. Therefore, the Company will re-seek authority by shareholders to purchase up to 10% of the Company's ordinary share capital as at 16 April 2018 at the AGM.

Shares held by employee benefit trusts

Data on the Group's share plans can be found at note 34.

Employee Share Incentive Plan (ESIP)

The Board approved the continuation of the tax-approved ESIP into its fourth year. The ESIP allows qualifying employees to acquire shares on beneficial terms in accordance with Schedule 2 and/or Schedule 3 to the Income Tax (Earnings and Pensions) Act 2003. Awards under the ESIP are satisfied by the issue of new ordinary shares by the Company.

Scheme participants make regular contributions to the ESIP directly from their salary up to a maximum of £150 per month (Partnership Shares) and under the rules of the scheme, the Company issues a matching share element on a 1:1 basis (Matching Shares).

Annual invitation reminders to participate in the evergreen scheme are sent to all eligible UK employees and information can be found on the intranet and the take-up as at 31 January 2018 was 33.2% of eligible employees.

Long Term Business Plan (LTBP)

During the 2016 financial year, the Company's Employee Benefit Trust (EBT) purchased Ordinary shares in the market at a cost of £15m which have been used in a long-term bonus plan (LTBP) to incentivise senior management below Board level and to align their interests with shareholders. Awards were made during the 2016 financial year.

Retention Scheme

On 19 December 2017, the Company issued two million conditional awards over market purchased Ordinary shares held by its EBT to certain key managers who were already in the LTBP scheme at nil cost.

Further details of the LTBP and Retention Scheme are set out in note 34. Each Ordinary share purchased and/or awarded under each plan carries the right to one vote at general meetings of the Company.

Senior Management Plan (SMP)

Certain of the Class A2, B2 and C2 MVP shares representing 14.2% of all MVP shares were issued to the Company's Employee Benefit Trust (EBT) and any ordinary shares resulting from the conversion of such MVP shares would be used for the benefit of certain of the senior management team below Board, subject to satisfaction of specified performance criteria at the absolute discretion of the Remuneration Committee.

Performance Share Plan (PSP)

On 27 October 2017, the Board announced that options over a total of 1,148,606 ordinary shares were awarded pursuant to the 2015 PSP and a supplementary award. Awards for Executive Directors are in line with the shareholder approved Remuneration Policy. Further awards to senior management were made on 19 December 2017 over approximately £4 million ordinary shares. The options were granted at nil cost and will be subject to the satisfaction of performance conditions. Subject to a holding period, the options will normally be exercisable from the third anniversary of the grant date until the tenth anniversary.

SUBSTANTIAL SHAREHOLDINGS

As at 31 January 2018, the Company has been notified in accordance with the Disclosure and Transparency Rules (DTR 5) of the following interests in 3% or more of the issued share capital of the Company:

Name of shareholder	Number of shares	% shareholding
Parvus Asset Management Europe Limited	151,917,183	24.88%
The Capital Group Companies, Inc.	87,485,945	14.32%
Woodford Investment Management	86,698,420	14.19%
Deutsche Bank AG	37,413,646	6.13%
BlackRock, Inc.	37,153,815	6.08%
Citigroup Global Markets Limited	32,298,146	5.29%
Standard Life Investment (Holdings) Limited	Below 5%	Below 5%
Goldman Sachs	27,784,771	4.55%
Classic Fund Management AG	18,432,641	3.02%

Since 31 January 2018, the Company has been notified in accordance with DTR5 of changes in the following interests:

Woodford Investment Management LLP	91,850,320	15.02%
Deutsche Bank AG	54,929,543	8.99%
Citigroup Global Markets Limited	36,102,007	5.90%
Merrill Lynch International	32,681,626	5.34%
Liontrust Investment Partners LLP	31,263,813	5.11%
Classic Fund Management AG	24,803,145	4.06%
BlackRock, Inc.		Below 5%
Cleveland Square Limited	18,390,488	3.01%

Except for those listed above, we are not aware of any ordinary shareholders with interests of 3% or more in the issued share capital of the Company. We have not been notified of any other changes to the notifiable voting rights in its shares up to 16 April 2018.

Interest in voting rights

All of the issued (and outstanding) ordinary shares of the Company have equal voting rights, with one vote per share. None of the ordinary shares carry any special voting rights with regard to control of the Company. Other than holding periods that may be imposed on ordinary shares from awards under share schemes, the Group is not aware of any agreements between holders of securities that may result in restrictions on the transfer of ordinary shares.

The Notice of AGM specifies deadlines for exercising voting rights and appointing a proxy or proxies to vote in relation to resolutions to be passed at the AGM. The relevant proxy votes are counted and the numbers for, against or withheld in relation to each resolution are announced at the AGM and published on the Company's website after the meeting.

Full voting rights are set out in the Company's Articles of Association (the Articles) and in the explanatory notes that accompany the Notice of the 2018 AGM. These documents are available on the Company's website www.theaapl.com.

The total voting rights figure applicable at 16 April 2018 is 611,515,571 ordinary shares.

Dividend Reinvestment Plan (DRIP)

The Company offers a dividend reinvestment plan to shareholders as a cost-efficient way of increasing their shareholding in the Company.

Directors

The membership of the current Board and biographical details are given on pages 52 to 53.

Appointment and replacement of Directors This is governed by the Articles, the Act, the Code and related legislation.

Directors' powers The business of the Company is managed by the Board who may exercise all powers of the Company, subject to the Articles, the Act and any directions given by special resolution of shareholders.

The Board is authorised to issue and allot shares, and to undertake purchase of shares, subject to shareholder approval at the AGM.

Directors' interests The interests of Directors and their immediate families in the shares of the Company, along with details of the long-term incentives awarded to Executive Directors are contained in the Directors' Remuneration Report set out on pages 75 to 88.

No Directors have beneficial interests in the shares of any subsidiary company. Further details relating to the MVP shares and PSP awards can be found on pages 84 to 85.

Directors' indemnities The Company maintains Directors' and officers' liability insurance, which gives appropriate cover for any legal action brought against its Directors and officers. The Company has also granted indemnities to each of its Directors and the Company Secretary to the extent permitted by law. Qualifying third-party indemnity provisions (as defined by section 234 of the Act) were in force during the year ended 31 January 2018 and remain in force, in relation to certain losses and liabilities which the Directors or Company Secretary may incur to third parties in the course of acting as Directors or Company Secretary or employees of the Company or any associated company.

Directors' conflicts of interest The Group has procedures in place for managing conflicts of interest. Should a Director become aware that they, or their connected parties, have an interest in an existing or proposed transaction with the AA, they must notify the Board in writing or at the next Board meeting. Internal controls are in place to ensure that any related party transactions involving Directors, or their connected parties, are conducted on an arm's length basis. Directors have a continuing duty to update any changes to these conflicts. The Directors consider the conflicts of interest procedures to have operated effectively during the year.

Independence of Directors The Board has reviewed the independence of each Non-Executive Director and considers them to be independent of management and free from business relationships that could interfere with the exercise of independent judgement. The Chairman was independent on appointment to that role and so is considered independent by the Board.

Articles of Association

Any amendment of the Company's Articles of Association requires shareholder approval in accordance with applicable legislation.

Minor amendments are being proposed at this year's AGM on 7 June 2018. Further details are contained in the Notice to Shareholders which is available on our website.

Significant agreements change of control

The Company is not party to any significant agreements that would take effect, alter or terminate following a change of control of the Company. However, some of our B2B contracts include change of control provisions in limited circumstances. The Company does not have agreements with any Director or officer that would provide compensation for loss of office or employment resulting from a takeover except that provisions of the Company's share plans and the MVP shares may cause awards and options granted under such arrangements to vest on a takeover.

Going concern and viability statement

Having carried out a comprehensive review of the business, regarding its financial position, future forecasts and the borrowing facilities available, the Directors confirm that they have a reasonable expectation that the AA has adequate resources to continue in operational existence for the foreseeable future. Therefore, the Directors continue to adopt the going concern basis in preparing the financial statements for the year ended 31 January 2018.

Our viability statement is set out on page 31.

Cautionary statement

This Annual Report contains forward-looking statements. These forward-looking statements are not guarantees of future performance, rather they are based on current views and assumptions as at the date of this Annual Report. These assumptions are made in good faith based on the information available at the time of the approval of this report. These statements should be treated with caution due to the inherent risks and uncertainties underlying any such forward-looking information. The Board has no obligation to update these forward looking statements.

Employment

The AA is an equal opportunities employer and has established best practice procedure, from recruitment and selection, through training and development, performance reviews and promotion to retirement. We promote an environment free from discrimination, harassment and victimisation, where everyone will receive equal treatment regardless of gender, colour, ethnic or national origin, disability, age, marital status, sexual orientation or religion.

Political donations

No political donations were made during the year ended 31 January 2018 (2017: £nil). The AA has a policy of not making donations to political organisations or independent election candidates or incurring political expenditure anywhere in the world as defined by relevant legislation.

Disclosures required under Listing Rule 9.8.4

In accordance with Listing Rule 9.8.4(12) and Listing Rule 9.8.4(13), we note that the Trustees of the AA plc 2015 Employee Benefit Trust have waived their right to receive dividends on the Ordinary shares comprised in the Trust Fund, being 4,111,423 ordinary shares as at 31 January 2018, under the terms of the Trust Deed.

There are no further disclosures required to be made under Listing Rule 9.8.4.

Directors' Report

continued

Auditors

Ernst & Young LLP have been the Group's auditor since the audit for the year ended 31 January 2008. In recognition of the FRC Ethical Standard 2016, in March 2017 the Audit Committee and Board commenced a competitive tender process for external audit services. The formal audit tender process took place during the year and resulted in the Audit Committee making a recommendation for PwC to be appointed as the new auditor of the Company. The appointment is with effect from the 2019 financial year, with the first reporting for the six months to 31 July 2018. Shareholder approval for this appointment will be sought at the upcoming AGM on 7 June 2018.

PwC has signified its willingness to be appointed as statutory auditor of the AA for the 2019 financial year and both the Board and Audit Committee are satisfied that PwC is independent and there are adequate safeguards in place to safeguard its objectivity.

Disclosure of information to the auditor

So far as the Directors are aware, there is no relevant audit information that has not been brought to the attention of the Company's auditor during the audit process. Each Director has taken all reasonable steps to make himself or herself aware of any relevant audit information and to establish that such information was provided to the auditor.

2018 Annual General Meeting

The Company's AGM will be held at the offices of Freshfields Bruckhaus Deringer LLP, Northcliffe House, 26-28 Tudor Street, London, EC4Y 0BQ on 7 June 2018 at 12 noon.

The Notice convening the 2018 AGM is contained in a circular sent to shareholders. Full details of all resolutions to be proposed are provided in this circular. The Directors consider that all of the resolutions set out are in the best interests of the Company and its shareholders as a whole. The Directors will be voting in favour of them and unanimously recommend that shareholders vote in favour of each of them.

Responsibilities of the Directors

The Directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations. Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have prepared the Group financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU and the Company financial statements in accordance with Financial Reporting Standard (FRS) 101. Under company law, the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and the Company and of the profit or loss of the Group for that period.

In preparing these financial statements, the Directors are required to:

- › select suitable accounting policies and then apply them consistently;
- › make judgements and accounting estimates that are reasonable and prudent;
- › state whether applicable IFRS as adopted by the EU have been followed, subject to any material departures disclosed and explained in the financial statements; and
- › prepare the Group's and Company's financial statements on a going concern basis, unless it is inappropriate to do so.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group's and Company's transactions and disclose with reasonable accuracy at any time the financial position of the AA and enable them to ensure that the financial statements comply with the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation. The Directors are also responsible for safeguarding the assets of the AA and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Responsibility statement of the Directors in respect of the Annual Report and financial statements

Each of the Directors as at the date of the Annual Report (as noted on pages 52 to 53) confirm that to the best of their knowledge:

- › the Group and Company financial statements, which have been prepared in accordance with IFRS and FRS101 respectively, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole;
- › the Strategic Report and Directors' Report on page 12 and page 89 respectively include a fair review of the development and performance of the business and the position of the Group, together with a description of the principal risks and uncertainties that it faces; and
- › the Annual Report, taken as a whole, is fair, balanced and understandable and provides the necessary information for shareholders to assess the Group's performance, business model and strategy.

A copy of the financial statements of the Group is placed on the Company's website at www.theaapl.com. The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Information published on the internet is accessible in many countries with different legal requirements. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

The Statement of Directors' Responsibilities was approved by the Board of Directors on 16 April 2018 and signed on its behalf by the Company Secretary:



Mark Millar
Company Secretary

16 April 2018

Financial Statements

for the year ended 31 January 2018

Our Business

Our Performance

Governance

Financial Statements

Independent Auditor's Report

to the members of AA plc

Opinion

In our opinion:

- › AA plc's Group financial statements and parent Company financial statements (the "financial statements") give a true and fair view of the state of the Group's and of the parent Company's affairs as at 31 January 2018 and of the Group's profit for the year then ended;
- › the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union;
- › the parent Company financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, including FRS 101 "Reduced Disclosure Framework"; and
- › the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

We have audited the financial statements of AA plc which comprise:

Group

- › Consolidated statement of financial position as at 31 January 2018
- › Consolidated income statement for the year then ended
- › Consolidated statement of comprehensive income for the year then ended
- › Consolidated statement of changes in equity for the year then ended
- › Consolidated statement of cash flows for the year then ended
- › Related notes 1 to 36 to the financial statements, including a summary of significant accounting policies

Parent Company

- › Statement of financial position as at 31 January 2018
- › Statement of changes in equity for the year then ended
- › Related notes 1 to 11 to the financial statements including a summary of significant accounting policies

The financial reporting framework that has been applied in the preparation of the Group financial statements is applicable law and IFRSs as adopted by the European Union. The financial reporting framework that has been applied in the preparation of the parent Company financial statements is applicable law and United Kingdom Generally Accepted Accounting Practice.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report below. We are independent of the Group and parent Company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard as applied to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Use of our report

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Conclusions relating to principal risks, going concern and viability statement

We have nothing to report in respect of the following information in the annual report, in relation to which the ISAs (UK) require us to report to you whether we have anything material to add or draw attention to:

- › the disclosures in the annual report set out on pages 34 to 37 that describe the principal risks and explain how they are being managed or mitigated;
- › the directors' confirmation set out on page 68 in the annual report that they have carried out a robust assessment of the principal risks facing the entity, including those that would threaten its business model, future performance, solvency or liquidity;
- › the directors' statement set out on page 91 in the financial statements about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them, and their identification of any material uncertainties to the entity's ability to continue to do so over a period of at least twelve months from the date of approval of the financial statements;
- › whether the directors' statement in relation to going concern required under the Listing Rules in accordance with Listing Rule 9.8.6R(3) is materially inconsistent with our knowledge obtained in the audit; or
- › the directors' explanation set out on page 31 in the annual report as to how they have assessed the prospects of the entity, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the entity will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

Overview of our audit approach

Key audit matters

- › Revenue recognition
- › Valuation of net pension scheme liability
- › Goodwill impairment

Audit scope

We performed an audit of the complete financial information of the Roadside Assistance and Insurance Services components (in line with the previous segmental view of the Group detailed in note 2 of the consolidated financial statements) and audit procedures on specific balances of the remaining components.

The components where we performed full or specific audit procedures accounted for 98% of the Group's earnings before interest, tax, depreciation and amortisation (Trading EBITDA) adjusted for exceptional items, 95% of the Group's Revenue and 93% of the Group's Total assets.

Materiality

Overall Group materiality of £7.4m which represents approximately 2% of the Group Trading EBITDA adjusted for exceptional items.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team. These matters were addressed in the context of our audit of the financial statements as a whole, and in our opinion thereon, and we do not provide a separate opinion on these matters.

Risk	Our response to these risks	Key observations communicated to the Audit Committee
Revenue recognition (£959m, PY comparative £940m) Refer to the Audit Committee Report (page 72) and accounting policy (note 1.3(m))		
<p>The basis of recognising revenue differs between the various products and services provided by the Group, as set out in accounting policy 1.3(m).</p> <p>Management has previously identified issues with the way in which an underlying system generates accounting entries for processing and deferring revenue from the personal roadside business, and has implemented additional procedures to ensure the accurate recording of such revenue.</p> <p>As such we consider that the deferral and subsequent recognition of revenue generated from the personal roadside business presents an increased risk of error or potential management override.</p>	<ul style="list-style-type: none"> › We performed full and specific scope audit procedures over this risk area which covered 95% of the Group's revenue. › We considered the Group's accounting policies in respect of revenue recognition to determine whether they appropriately reflected the requirements of IAS 18 and IFRS 4. › We assessed the design, implementation and operating effectiveness of key controls over revenue recognition and tested controls over revenue processing for the principal roadside assistance and insurance income streams. › We tested IT general controls that support the systems that process and record revenue for the roadside assistance, insurance and driving services income streams. › Specifically, for the system issues where management has implemented additional procedures, we tested controls over those procedures. We checked the completeness of data used in the calculation of revenue, tested the methodology used to generate accounting entries by re-performing a sample of calculations and verified that the resulting accounting entries had been accurately processed. › We performed tests of detail to assess whether the revenue recognition practices adopted complied with the stated accounting policies. We tested a sample of personal roadside assistance revenue transactions to confirm that revenue had been deferred in a manner consistent with the relevant contract and a sample of insurance broking transactions to confirm that all services under the contract had been performed at the point at which revenue was recognised. › We inspected a sample of journal entries for any evidence of management override and obtained support for individually unusual and/or material revenue journals. › We performed analytical procedures to compare revenue recognised with our expectations from past experience, management's forecasts and our understanding of product features and terms. In doing so we assessed whether deferred revenue from the personal roadside business as at 1 February 2017 had been appropriately released to revenue during the year. › We performed cut-off testing to confirm that revenue has been recorded in the correct period. 	<p>We are satisfied that appropriate revenue recognition policies have been adopted and complied with.</p> <p>Based on additional procedures carried out by management and the results of our own controls and substantive testing we are satisfied that revenue transactions have been appropriately recorded.</p>

Independent Auditor's Report

continued

Risk	Our response to these risks	Key observations communicated to the Audit Committee
<p>Valuation of the net pension scheme liability (£240m, PY comparative £395m)</p> <p>Refer to the Audit Committee Report (page 72); accounting policy (note 1.3(l)) and note 25 of the consolidated financial statements</p> <p>The Group operates three defined benefit pension schemes, the most significant of which is the AA UK defined benefit scheme (AAUK). We consider the valuation of the AAUK net pension liability to be a significant risk as:</p> <ul style="list-style-type: none"> › The actuarial assumptions used to value the pension scheme liabilities are judgemental and sensitive; › The schemes hold some complex and illiquid assets for which there are no quoted prices. Prices are obtained directly from the relevant investment managers who apply judgement in valuing those assets. <p>Due to the significance of the value of the AAUK pension obligation, a small change in actuarial assumptions may result in a material difference to the amounts reported.</p> <p>Furthermore, during the current financial year, the Group closed the Final Salary section of AAUK, effective 1 July 2017. All active members moved to the CARE section removing the salary link to the benefits. In addition, pension indexation in the CARE section has been linked to CPI inflation, rather than RPI inflation.</p>		
<p>Goodwill impairment (carrying value £1,170m, PY comparative £1,173m)</p> <p>Refer to the Audit Committee Report (page 72), accounting policy (note 1.3(i)) and note 11 of the consolidated financial statements</p> <p>The goodwill balance as at 31 January 2018 is significant based on its size relative to the total assets of the Group. The AA plc goodwill arising on consolidation represents the excess of the cost of acquisition over the Group's interest in the fair value of the identified assets and liabilities at the date of acquisition in 2004. Management analyses discounted cash flows at the Cash Generating Units ('CGU') level to calculate the value in use for each CGU as required by IAS 36. This calculation represents a significant estimate including judgements related to future Trading EBITDA growth and discount rate assumptions. In the current financial year the Group acquired Used Car Sites Limited. This resulted in the recognition of £25m goodwill as at 31 January 2018. As detailed in note 11 of the consolidated financial statements, the goodwill allocated to the Driving School CGU (£26m) was fully impaired in the current financial year.</p>		
	<ul style="list-style-type: none"> › We performed specific scope audit procedures over this risk area which covered 100% of the risk amount. › We understood and walked through management's controls in respect of the selection of key assumptions related to the valuation of actuarial liabilities and the valuation of scheme assets. › Using external data we verified the appropriateness of the key actuarial assumptions used by management in determining the pension obligation under IAS 19(R) as detailed in note 25 of the consolidated financial statements. › We determined whether the assumptions used met the requirements of IFRS and were in line with market practice, as well as the specific circumstances of the schemes and their participants. This included a comparison of life expectancy with relevant mortality tables, benchmarking inflation and discount rates against external market data, considering changes in historical assumptions and evaluating the independence, qualifications and results of work performed by management's experts involved in the valuation process. We used our pension valuation experts to assist us with these procedures. › We confirmed the appropriate accounting treatment of the AAUK plan amendment. › We obtained net asset value (NAV) statements in respect of the schemes' investments directly from the fund administrator and reconciled them to both the scheme's custody records and the Group financial statements. › Where applicable we reviewed administrator controls reports for controls over valuation of complex assets. › For the complex assets we obtained and reviewed a sample of audited fund financial statements to assess whether the NAV was appropriate. › We tested the assets held in equity markets and confirmed the valuation of those equities. › We tested the data used to perform scheme valuations to gain comfort that the data is complete and accurate and agrees to underlying payroll records. › We reviewed the disclosures relating to the defined benefit schemes. 	<p>We are satisfied that the values of assets held within the scheme are appropriately supported.</p> <p>We concluded that assumptions used to determine the defined benefit obligation fall within an acceptable range.</p> <p>We concluded that accounting treatment of the AAUK plan amendment is in line with IAS19(R).</p>
	<ul style="list-style-type: none"> › We performed full scope audit procedures over this risk area. › We examined management's impairment model, which included an assessment of discounted cash flows, to understand the significant assumptions used in the impairment test for each CGU. › We engaged our valuation experts to assess the reasonableness of the discount rate by considering the Group specific circumstances as well as comparable companies from similar sectors. › We performed sensitivity analysis to assess the impact of certain key variables on levels of headroom, including discount rate and Trading EBITDA growth assumptions. › We confirmed the appropriate accounting treatment in respect of goodwill relating to the acquired Used Car Sites Limited (trading as 'AA Cars'). › We confirmed compliance with the Group's accounting policy. 	<p>We are satisfied that the basis for the Driving School CGU impairment is appropriate and the impairment assessment is in line with the Group accounting policy.</p> <p>Based on our procedures, which included additional sensitivity analysis, we are satisfied that no additional impairment of the recorded goodwill has been identified.</p>

Key audit matters (continued)

In the prior year, our auditor's report included a key audit matter in relation to Recognition and valuation of provisions: Duplicate breakdown cover. In the current year we do not consider this risk area to represent a key audit matter. As detailed in note 21 of the consolidated financial statements, the majority of the provision balance was utilised during the current financial year and limited judgement and estimation uncertainty remains in relation to the provision as at 31 January 2018.

An overview of the scope of our audit

Tailoring the scope

Our assessment of audit risk, our evaluation of materiality and our allocation of performance materiality determine our audit scope for each entity within the Group. Taken together, this enables us to form an opinion on the consolidated financial statements.

In assessing the risk of material misstatement to the Group financial statements, and to ensure we had adequate quantitative coverage of significant accounts in the financial statements, our audit scope focused on the two largest components, Roadside Assistance and Insurance Services, which were subject to a full scope audit for the year ended 31 January 2018. For the remaining components (Driving Services and Insurance Underwriting) and the statutory entities containing the Group's borrowings and related hedging instruments, pension scheme balances, insurance technical provisions and head office costs, specific audit procedures were performed that were impacted by our assessed risks of material misstatement. The scope of our audit is based on the reporting components of the Group in line with the previous segmental view of the Group management as detailed in note 2.

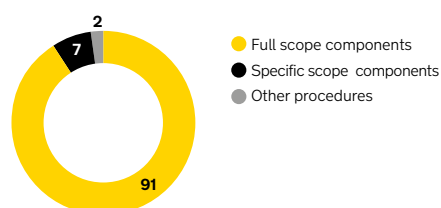
The components for which we performed full scope audits accounted for 91% (2017: 93%) of the Group's revenue, 91% (2017: 92%) of the Group's Trading EBITDA and 60% (2017: 61%) of the Group's total assets. The specific scope component contributed 4% (2017: 4%) of the Group's Revenue, 7% (2017: 7%) of the Group's Trading EBITDA and 33% (2017: 36%) of the Group's total assets. The specific scope components include the statutory entities containing the Group's borrowings and related hedging instruments, pension scheme balances and insurance technical provisions where specific audit procedures were performed based on our assessed risks of material misstatement. The audit scope of these components may not have included testing of all significant accounts of the component but will have contributed to the coverage of significant accounts tested for the Group.

The remaining components together represent 2% (2017: 1%) of the Group's Trading EBITDA. For these components, we performed other procedures, including analytical review, testing of consolidation journals and intercompany eliminations to respond to any potential risks of material misstatement to the Group financial statements.

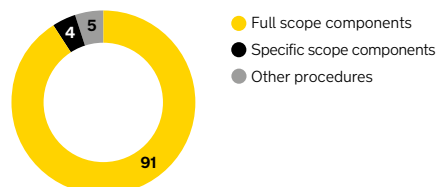
Items not included in the Trading EBITDA coverage include the difference between the cash contributions to the pension schemes for ongoing service and the calculated annual service cost and share-based payments. Pensions and Incentive Schemes have been subject to specific substantive audit procedures as set out in this report.

The charts below illustrate the coverage obtained from the work performed by our audit teams.

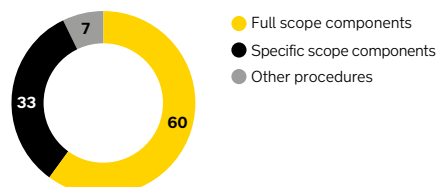
TRADING EBITDA (%)



REVENUE (%)



TOTAL ASSETS (%)



Independent Auditor's Report

continued

Involvement with component teams

In establishing our overall approach to the Group audit, we determined the type of work that needed to be undertaken at each of the components by us, as the primary audit engagement team, or by the component auditors operating under our instruction.

The Insurance component team is responsible for the audit of the Insurance Services and Insurance Underwriting segments. The Group audit team is responsible for the audit of the Group Function and all other components.

The Group audit team provided detailed audit instructions to the component team which included guidance on areas of focus, including the relevant risks of material misstatement detailed above, and set out the information required to be reported to the Group team.

The primary team interacted regularly with the component teams where appropriate during various stages of the audit, reviewed key working papers and were responsible for the scope and direction of the audit process. The Group team attended the closing meetings with the management of the Insurance component and attended key audit committee meetings. This, together with the additional procedures performed at Group level, gave us appropriate evidence for our opinion on the Group financial statements.

Our application of materiality

We apply the concept of materiality in planning and performing the audit, in evaluating the effect of identified misstatements on the audit and in forming our audit opinion.

Materiality

The magnitude of an omission or misstatement that, individually or in the aggregate, could reasonably be expected to influence the economic decisions of the users of the financial statements. Materiality provides a basis for determining the nature and extent of our audit procedures.

We determined materiality for the Group to be £7.4 million (2017: £7.6 million), which is approximately 2% (2017: approximately 2%) of Trading EBITDA adjusted for exceptional items. We base our materiality on a Trading EBITDA performance measure as Trading EBITDA has been the key metric used by management in measuring and reporting on the performance of the business during the year. In presenting its measure of Trading EBITDA, management adjusts Trading EBITDA for non-recurring items and also certain recurring items including the difference between the cash contributions to the pension schemes for ongoing service and the calculated annual service cost and share-based payments. In calculating materiality, we have adjusted Trading EBITDA only for exceptional items which we considered to be non-recurring. This provided a basis for determining the nature, timing and extent of risk assessment procedures, identifying and assessing the risk of material misstatement and determining the nature, timing and extent of further audit procedures.

Starting basis	› Starting point – £391m Group Trading EBITDA
Adjustments	› £17m recurring items, the difference between the cash contributions to the pension schemes for ongoing service and the calculated annual service cost and share-based payments
Materiality basis	› Materiality basis – £374m adjusted Group Trading EBITDA › Materiality of £7.4m (approximately 2% of the materiality basis)

During the course of our audit, we reassessed initial materiality. Our final calculated materiality did not result in any substantive change in our audit procedures.

Performance materiality

The application of materiality at the individual account or balance level. It is set at an amount to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality.

On the basis of our risk assessments, together with our assessment of the Group's overall control environment, our judgement was that performance materiality was 50% (2017: 50%) of our planning materiality, namely £3.7m (2017: £3.8m). Our objective in adopting this approach is to ensure that total uncorrected and undetected audit differences do not exceed our materiality of £7.4m for the financial statements as whole.

Audit work at components for the purpose of obtaining audit coverage over significant financial statement accounts is undertaken based on a percentage of total performance materiality. The performance materiality set for each component is based on the relative scale and risk of the component to the Group as a whole and our assessment of the risk of misstatement at that component. In the current year, the range of performance materiality allocated to components was £0.7m to £2.5m (2017: £0.8m to £2.8m).

Reporting threshold

An amount below which identified misstatements are considered as being clearly trivial.

We agreed with the Audit Committee that we would report to them all uncorrected audit differences in excess of £0.4m (2017: £0.4m), which is set at 5% of planning materiality, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations in forming our opinion.

Other information

The other information comprises the information included in the annual report set out on pages 1 to 92, including the Strategic Report and Directors' Report, other than the financial statements and our auditor's report thereon. The directors are responsible for the other information.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in this report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of the other information, we are required to report that fact.

We have nothing to report in this regard.

In this context, we also have nothing to report in regard to our responsibility to specifically address the following items in the other information and to report as uncorrected material misstatements of the other information where we conclude that those items meet the following conditions:

- › **Fair, balanced and understandable set out on page 92** – the statement given by the directors that they consider the annual report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's performance, business model and strategy, is materially inconsistent with our knowledge obtained in the audit; or
- › **Audit committee reporting set out on page 70** – the section describing the work of the audit committee does not appropriately address matters communicated by us to the audit committee; or
- › **Directors' statement of compliance with the UK Corporate Governance Code set out on page 50** – the parts of the directors' statement required under the Listing Rules relating to the Company's compliance with the UK Corporate Governance Code containing provisions specified for review by the auditor in accordance with Listing Rule 9.8.10R(2) do not properly disclose a departure from a relevant provision of the UK Corporate Governance Code.

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006.

In our opinion, based on the work undertaken in the course of the audit:

- › the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- › the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the Group and the parent Company and its environment obtained in the course of the audit, we have not identified material misstatements in the Strategic Report or the Directors' Report.

We have nothing to report in respect of the following matters in relation to which the Companies Act 2006 requires us to report to you if, in our opinion:

- › adequate accounting records have not been kept by the parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- › the parent Company financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- › certain disclosures of directors' remuneration specified by law are not made; or
- › we have not received all the information and explanations we require for our audit.

Responsibilities of directors

As explained more fully in the Directors' Responsibilities Statement set out on page 92, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the Group and parent Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or the parent Company or to cease operations, or have no realistic alternative but to do so.

Independent Auditor's Report

continued

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Explanation as to what extent the audit was considered capable of detecting irregularities, including fraud

The objectives of our audit:

- › In respect to fraud, are; to identify and assess the risks of material misstatement of the financial statements due to fraud; to obtain sufficient appropriate audit evidence regarding the assessed risks of material misstatement due to fraud, through designing and implementing appropriate responses; and to respond appropriately to fraud or suspected fraud identified during the audit. However, the primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the Group and management; and
- › In respect to irregularities, considered to be non-compliance with laws and regulations, are to obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations generally recognized to have a direct effect on the determination of material amounts and disclosures in the financial statements ('direct laws and regulations'), and perform other audit procedures to help identify instances of non-compliance with other laws and regulations that may have a material effect on the financial statements. We are not responsible for preventing non-compliance with laws and regulations and our audit procedures cannot be expected to detect non-compliance with all laws and regulations.

Our approach was as follows:

- › We obtained a general understanding of the legal and regulatory frameworks that are applicable to the Group and the parent Company and determined that the most significant are Companies Act 2006, the UK Corporate Governance Code, UK Tax Legislation and the financial reporting framework. Our considerations of other laws and regulations that may have a material effect on the financial statements included permissions and supervisory requirements of the Prudential Regulation Authority ("PRA") and the Financial Conduct Authority ("FCA").
- › We obtained a general understanding of how the Company is complying with those frameworks by making enquiries of management, internal audit, and those responsible for legal and compliance matters. We also reviewed correspondence between the Company and UK regulatory bodies; reviewed minutes of the Board and its Committees; and gained an understanding of the Company's approach to governance, demonstrated by the Board's approval of the Group's governance framework and the Board's review of the Group's risk management framework and the Group's system of internal controls.
- › For direct laws and regulations, we considered the extent of compliance with those laws and regulations as part of our procedures on the related financial statement items.

› For both direct and other laws and regulations our procedures involved: making enquiry of those charged with governance and senior management for their awareness of any non-compliance of laws or regulations, inquiring about the policies that have been established to prevent non-compliance with laws and regulations by officers and employees, inquiring about the Group's methods of enforcing and monitoring compliance with such policies, inspecting significant correspondence with the FCA and PRA.

› The Group's Insurance component operates in the insurance industry which is a highly regulated environment. As such the Senior Statutory Auditor considered the experience and expertise of the engagement team to ensure that the team had the appropriate competence and capabilities, which included the use of specialists where appropriate.

› We assessed the susceptibility of the Group's and the parent Company's financial statements to material misstatement, including how fraud might occur by considering the controls implemented to address risks identified by the Group, or that otherwise seek to prevent, deter or detect fraud. We also considered areas of significant judgement, including complex transactions, performance targets and economic or external pressures and the impact these have on the control environment. Where this risk was considered to be higher, we performed audit procedures to address each identified fraud risk. These procedures included testing manual journals and were designed to provide reasonable assurance that the financial statements were free from fraud or error.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at <https://www.frc.org.uk/auditorsresponsibilities>. This description forms part of our auditor's report.

Other matters we are required to address

- › We were appointed by the Company in June 2007 to audit the financial statements for the year ending 31 January 2008 and subsequent financial periods.
- › The period of total uninterrupted engagement with the Company including previous renewals and reappointments is eleven years, covering the years ending 31 January 2008 to 31 January 2018, including the period of our audit engagement before the Company's Initial Public Offering on 26 June 2014.
- › The non-audit services prohibited by the FRC's Ethical Standard were not provided to the Group or the parent Company and we remain independent of the Group and the parent Company in conducting the audit.
- › The audit opinion is consistent with the additional report to the audit committee.

Kathryn Barrow (Senior statutory auditor)

for and on behalf of Ernst & Young LLP, Statutory Auditor
London

16 April 2018

1 The maintenance and integrity of the AA plc web site is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the web site.

2 Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Consolidated income statement

for the year ended 31 January

	Note	2018 £m	2017 £m
Continuing operations			
Trading Revenue	2	959	940
Exceptional revenue provision	5	1	(7)
Group Revenue	2	960	933
Cost of sales		(360)	(341)
Gross profit		600	592
Administrative and marketing expenses		(292)	(309)
Share of (loss)/profit of joint venture and associates, net of tax		(1)	1
Operating profit	4	307	284
Trading EBITDA	2	391	403
Share-based payments	34	(7)	(12)
Pension service charge adjustment	2	(10)	(8)
Amortisation and depreciation	11,13	(70)	(67)
Operating profit before exceptional items		304	316
Exceptional operating items	5	3	(32)
Operating profit	4	307	284
Finance costs	6	(167)	(185)
Finance income	7	1	1
Profit before tax		141	100
Tax expense	9	(30)	(26)
Profit for the year from continuing operations		111	74
Discontinued operations			
Profit for the year from discontinued operations	3	-	80
Profit for the year		111	154

	Note	2018 pence	2017 pence
Earnings per share from profit for the year			
Basic from total operations	10	18.2	25.3
Basic from continuing operations	10	18.2	12.2
Basic from discontinued operations	10	-	13.1
Diluted from total operations	10	18.2	25.3
Diluted from continuing operations	10	18.2	12.2
Diluted from discontinued operations	10	-	13.1

The accompanying notes are an integral part of this consolidated income statement.

Consolidated statement of comprehensive income

for the year ended 31 January

	Note	2018 £m	2017 £m
Profit for the year		111	154
Other comprehensive income on items that may be reclassified to profit and loss in subsequent years			
Exchange differences on translation of foreign operations		(1)	2
Effective portion of changes in fair value of cash flow hedges		8	13
Tax effect	9	(3)	(1)
		4	14
Other comprehensive income on items that will not be reclassified to profit and loss in subsequent years			
Remeasurement on gains/(losses) on defined benefit schemes	25	120	(99)
Tax effect	9	(21)	17
		99	(82)
Total other comprehensive income		103	(68)
Total comprehensive income for the year		214	86

The accompanying notes are an integral part of this consolidated statement of comprehensive income.

Consolidated statement of financial position

as at 31 January

	Note	2018 £m	2017 £m
Non-current assets			
Goodwill and other intangible assets	11	1,300	1,283
Property, plant and equipment	13	127	131
Investments in joint ventures and associates	14	8	10
Other receivables	16	3	–
Deferred tax assets	9	31	62
		1,469	1,486
Current assets			
Inventories	15	7	6
Trade and other receivables	16	201	195
Cash and cash equivalents	17	150	211
		358	412
Total assets		1,827	1,898
Current liabilities			
Trade and other payables	18	(528)	(520)
Current tax payable		(10)	(11)
Provisions	21	(13)	(19)
		(551)	(550)
Non-current liabilities			
Borrowings and loans	19	(2,736)	(2,819)
Finance lease obligations	29	(16)	(20)
Defined benefit pension scheme liabilities	25	(240)	(395)
Provisions	21	(4)	(11)
Deferred consideration	18	(11)	–
Insurance technical provisions	22	(24)	(16)
		(3,031)	(3,261)
Total liabilities		(3,582)	(3,811)
Net liabilities		(1,755)	(1,913)
Equity			
Share capital	23	1	1
Share premium	24	406	403
Own shares	24	(29)	(26)
Currency translation reserve	24	–	1
Cash flow hedge reserve	24	5	2
Retained earnings	24	(2,138)	(2,294)
Total equity attributable to equity holders of the parent		(1,755)	(1,913)

Signed for and on behalf of the Board on 16 April 2018 by

Simon Breakwell
Chief Executive Officer

Martin Clarke
Chief Financial Officer

The accompanying notes are an integral part of this consolidated statement of financial position.

Consolidated statement of changes in equity

for the year ended 31 January

	Attributable to the equity holders of the parent						
	Share capital £m	Share premium £m	Own shares £m	Currency translation reserve £m	Cash flow hedge reserve £m	Retained earnings £m	Total £m
At 1 February 2016	1	399	(22)	(1)	(10)	(2,323)	(1,956)
Profit for the year	–	–	–	–	–	154	154
Other comprehensive income	–	–	–	2	12	(82)	(68)
Total comprehensive income	–	–	–	2	12	72	86
Dividends	–	–	–	–	–	(55)	(55)
Issue of share capital	–	4	–	–	–	–	4
Purchase of own shares	–	–	(4)	–	–	–	(4)
Share-based payments (see note 34)	–	–	–	–	–	12	12
At 31 January 2017	1	403	(26)	1	2	(2,294)	(1,913)
Profit for the year	–	–	–	–	–	111	111
Other comprehensive income	–	–	–	(1)	5	99	103
Total comprehensive income	–	–	–	(1)	5	210	214
Other reserves	–	–	–	–	(2)	2	–
Dividends	–	–	–	–	–	(56)	(56)
Issue of share capital	–	3	–	–	–	–	3
Purchase of own shares	–	–	(3)	–	–	–	(3)
At 31 January 2018	1	406	(29)	–	5	(2,138)	(1,755)

The accompanying notes are an integral part of this consolidated statement of changes in equity.

Consolidated statement of cash flows

for the year ended 31 January

	Note	2018 £m	2017 £m
Profit before tax from continuing and discontinued operations		141	184
Amortisation and depreciation	11,13	70	68
Net finance costs	6,7	166	184
Other adjustments to profit before tax		23	(62)
Working capital:			
(Increase) in trade and other receivables		(3)	(45)
(Decrease)/increase in trade and other payables		(8)	23
(Decrease)/increase in provisions		(6)	24
Difference between pension charge and cash contributions		(44)	(10)
Total working capital adjustments		(61)	(8)
Net cash flows from operating activities before tax		339	366
Tax paid		(23)	(21)
Net cash flows from operating activities		316	345
Investing activities			
Capital expenditure		(63)	(71)
Proceeds from sale of fixed assets		18	18
Acquisitions and disposals, net of cash acquired or disposed of		1	99
Interest received		1	1
Net cash flows (used in)/from investing activities		(43)	47
Financing activities			
Proceeds from borrowings		250	700
Issue costs on borrowings		(7)	(6)
Debt repayment premium and penalties		(11)	(30)
Repayment of borrowings		(328)	(766)
Refinancing transactions		(96)	(102)
Interest paid on borrowings		(136)	(143)
Payment of finance lease capital		(41)	(43)
Payment of finance lease interest		(5)	(7)
Dividends paid		(56)	(55)
Net cash flows used in financing activities		(334)	(350)
Net (decrease)/increase in cash and cash equivalents		(61)	42
Net foreign exchange differences		-	3
Cash and cash equivalents at 1 February		211	166
Cash and cash equivalents at 31 January	17	150	211

The cash flows from operating activities are stated net of cash outflows relating to exceptional items of £29m (2017: £15m). This relates to the cost of business transformation of £14m (2017: £11m), non-recurring costs of IT system implementation and cost restructuring activities of £5m (2017: £7m), costs of reimbursing customers who bought duplicate breakdown cover of £8m (2017: £nil) and a net cash outflow from onerous property lease provisions in respect of vacant properties of £2m (2017: inflow £3m).

Other adjustments to profit before tax of £23m (2017: outflow of £62m) include impairment of goodwill £27m (2017: £nil), profit on sale of home services business £6m (2017: £nil), profit on sale of Ireland £nil (2017: £77m), share of loss from joint ventures and associates of £1m (2017: profit of £1m), share-based payment charge of £7m (2017: £12m), profit on sale of fixed assets of £1m (2017 loss: £3m), credit for reversal of MVP share-based payment charge (see note 34) £7m (2017: £nil), loss on disposal of VVCR £1m (2017: £nil) and impairment of investment in joint ventures of £1m (2017: £1m).

Operating cash flows from discontinued operations were £nil (2017: £10m) (see note 3).

The accompanying notes are an integral part of this consolidated statement of cash flows.

Notes to the consolidated financial statements

1 Basis of preparation and accounting policies

1.1 General information

The consolidated financial statements for the year ended 31 January 2018 comprise the financial statements of AA plc ('the Company') and its subsidiaries (together referred to as 'the Group'). AA plc is a public limited company incorporated and domiciled in England and Wales.

These statements and the prior year comparatives have been presented to the nearest £million.

1.2 Basis of preparation

The Group has prepared these statements under International Financial Reporting Standards (IFRS) as adopted by the European Union, International Financial Reporting Interpretation Council (IFRIC) interpretations and those parts of the Companies Act 2006 applicable to companies reporting under IFRS.

These consolidated financial statements have been prepared under the historic cost convention as modified by the measurement of derivatives and liabilities for contingent consideration in business combinations at fair value.

a) Going concern

The Group is highly cash generative with a large proportion of its revenues coming from recurring transactions. The significant customer loyalty demonstrated by high renewal rates and lengthy customer tenure underpins this and in addition to the cash balances at the reporting date the Group has agreed undrawn credit facilities. The majority of the Group's borrowings are long term in nature with no borrowings due within 12 months from the date of signing of these financial statements. For the Group's longer term viability, it remains a key assumption of the Directors that the Group continues to have ready access to both public debt and equity markets to enable these borrowings to be easily refinanced in due course. The Directors have reviewed projected cash flows for a period of one year from the date of signing these financial statements and have concluded that the Group has sufficient funds to continue trading for this period and the foreseeable future. Therefore, the financial statements have been prepared using the going concern basis.

b) Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries). Control is achieved where the Company has rights to variable returns from its involvement with the entity and has the ability to influence those returns through its power over the entity.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate. Where necessary, adjustments are made to the financial statements of subsidiaries to bring the accounting policies into line with those used by the Group. All intra-group transactions, balances, income and expenses are eliminated on consolidation.

1.3 Accounting policies

The principal accounting policies are set out below.

a) Interests in joint ventures and associates

An associate is an entity over which the Group is in a position to exercise significant influence, but not control or joint control, through participating in the financial and operating policy decisions of the entity. Joint ventures are joint arrangements whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement.

The results, assets and liabilities of joint ventures and associates are incorporated in these financial statements using the equity method of accounting. Investments in joint ventures and associates are carried in the Group balance sheet at cost, including direct acquisition costs, as adjusted by post-acquisition changes in the Group's share of the net assets less any impairment losses.

b) Foreign currencies

These financial statements are presented in pound sterling, which is the currency of the primary economic environment in which the Group operates.

Transactions in currencies other than the functional currency of each consolidated undertaking are recorded at rates of exchange prevailing on the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated into the respective functional currency at rates of exchange ruling at the balance sheet date. Gains and losses arising on the translation of assets and liabilities are taken to the income statement.

The results of overseas operations are translated into sterling at average rates of exchange for the period. Exchange differences arising on the retranslation of the opening net assets of overseas operations are transferred to the Group's cumulative translation reserve in equity through other comprehensive income.

c) Business combinations and goodwill

All business combinations are accounted for by applying the acquisition method.

Costs related to the acquisition, other than those associated with the issue of debt or equity securities, are expensed as incurred.

Goodwill arising on consolidation represents the excess of the cost of acquisition over the Group's interest in the fair value of the identified assets and liabilities of a subsidiary at the date of acquisition. Goodwill is recognised as an asset at cost less accumulated impairment losses.

Any contingent consideration payable is recognised at fair value at the acquisition date, and subsequent changes to the fair value of the contingent consideration are recognised in profit or loss.

d) Intangible assets

Intangible assets other than goodwill which are acquired separately are stated at cost. The cost of intangible assets acquired in a business combination is their fair value as at the date of acquisition.

Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and impairment losses. Intangible assets with finite lives are amortised over the useful economic life.

e) Software and development costs

Software development expenditures on an individual project are recognised as an intangible asset when the Group can demonstrate:

- > The technical feasibility of completing the intangible asset so that it will be available for use or sale
- > Its intention to complete and its ability to use or sell the asset
- > How the asset will generate future economic benefits
- > The availability of resources to complete the asset
- > The ability to measure reliably the expenditure during development

Following initial recognition of the development expenditure as an asset, the cost model is applied. The asset is carried at cost less any accumulated amortisation and impairment losses. Amortisation of the asset begins when development is complete and the asset is available for use. It is amortised over its useful life of three to five years.

f) Property, plant and equipment

Land and buildings held for use in the production of goods and services or for administrative purposes are stated in the balance sheet at cost or fair value for assets acquired in a business combination less any subsequent accumulated depreciation and impairment losses. No capitalised interest is included in the cost of items of property, plant and equipment.

1 Basis of preparation and accounting policies (continued)

1.3 Accounting policies (continued)

Property, plant and equipment is stated at cost less accumulated depreciation and impairment losses. Such costs include costs directly attributable to making the asset capable of operating as intended. The cost of property, plant and equipment less their expected residual value is depreciated by equal instalments over their useful economic lives. These lives are as follows:

Buildings	50 years
Related fittings	3 – 20 years
Leasehold properties	over the period of the lease
IT systems (hardware)	3 – 5 years
Plant, vehicles and other equipment	3 – 10 years

Assets held under finance leases are depreciated on a straight line basis over the lease term.

g) Inventories

Inventories are stated at the lower of cost and net realisable value. Costs include all costs incurred in bringing each product to its present location and condition. Net realisable value is based on estimated selling price less any further costs expected to be incurred to completion and disposal.

h) Financial instruments

Financial assets and financial liabilities are recognised on the Group's balance sheet when the Group becomes a party to the contractual provisions of the instrument. They are classified according to the substance of the contractual arrangements entered into. At each reporting date the Group assesses whether there is any objective evidence that a financial asset or a group of financial assets is impaired.

Trade receivables and trade payables

Trade receivables and trade payables are not interest bearing and are recognised initially at fair value. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables.

Cash and cash equivalents

Cash and cash equivalents comprise cash balances and call deposits with an original maturity less than three months.

Debt instruments

Debt is initially recognised in the balance sheet at fair value less transaction costs incurred directly in connection with the issue of the instrument. Debt issue fees in respect of the instrument, including premiums and discounts on issue, are capitalised at inception and charged to the income statement over the term of the instrument using the effective interest method. Issue costs relating to the extinguishment of debt are charged to the profit and loss account immediately.

Equity instruments (share capital issued by the Group)

An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all its liabilities. Equity instruments are recognised at the fair value of proceeds received less direct issue costs.

Derivative financial instruments

The Group's capital structure exposes it to the financial risk of changes in interest rates and fuel prices. The Group uses interest rate and fuel swap contracts to hedge these exposures.

Derivative financial instruments are recorded in the balance sheet at fair value. The fair value of derivative financial instruments is determined by reference to market values for similar financial instruments. The gain or loss on remeasurement to fair value is recognised immediately in profit or loss unless they qualify for hedge accounting as described below.

Cash flow hedges

Changes in the fair value of derivative financial instruments that are designated as highly effective hedges of future cash flows are recognised in other comprehensive income. Any ineffective portion of the hedge is recognised immediately in the income statement. Amounts recognised in other comprehensive income are reclassified from equity to profit and loss (within finance costs) in the period when the hedged item affects profit or loss. When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss recognised in other comprehensive income at that time remains in equity and is reclassified when the hedged transaction is ultimately recognised in the income statement.

In order to qualify for hedge accounting, the Group is required to document from inception the relationship between the item being hedged and the hedging instrument and demonstrate that the hedge will be highly effective on an ongoing basis. This effectiveness testing is performed at each period end to ensure that the hedge remains highly effective.

i) Impairment of assets

The carrying amounts of the Group's non-financial assets, other than inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. In addition, goodwill and intangible assets not yet available for use are tested for impairment annually.

For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the cash generating units or "CGUs"). The goodwill acquired in a business combination is allocated to CGUs so that the level at which impairment is tested reflects the lowest level at which goodwill is monitored for internal reporting purposes.

The recoverable amount of an asset or cash generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

An impairment loss is recognised if the carrying amount of an asset or its CGU exceeds its estimated recoverable amount. Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of CGUs are allocated first to reduce the carrying amount of any allocated goodwill and then to reduce the carrying amounts of the other assets on a pro rata basis.

An impairment loss in respect of goodwill is not reversed. In respect of other assets, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

j) Leases

Finance leases transfer substantially all of the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Assets held under finance leases are recognised as assets of the Group at their fair value or, if lower, at the present value of the minimum lease payments, each determined at the inception of the lease. The corresponding liability to the lessor is shown as a financial liability. Lease payments are apportioned between finance charges and the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly to the income statement.

Rentals payable and receivable under operating leases are charged, or credited, to the income statement on a straight-line basis over the term of the relevant lease. Any incentives to enter into an operating lease are recognised evenly over the lease term.

Notes to the Consolidated Financial Statements

continued

1 Basis of preparation and accounting policies (continued)

1.3 Accounting policies (continued)

k) Provisions and contingent liabilities

A provision is required when the Group has a present legal or constructive obligation as a result of a past event and it is probable that settlement will be required of an amount that can be reliably estimated. Provisions are discounted where the impact is material. Material contingent liabilities are disclosed unless the transfer of economic benefits is remote. Contingent assets are only disclosed if an inflow of economic benefits is probable.

Provisions for restructuring costs are recognised when the Group has a detailed formal plan for the restructuring that has been communicated to affected parties.

For property leases, where a decision has been made prior to the year end to permanently vacate the property, provision is made for future rent and similar costs net of any rental income expected to be received up to the estimated date of final disposal.

l) Retirement benefit obligation

The Group's position in respect of defined benefit pension plans is calculated by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value, and the fair value of any plan assets (at bid price) is deducted. The Group determines the net interest on the net defined benefit liability for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the net defined benefit liability.

The discount rate is the yield at the reporting date on bonds that have a credit rating of at least AA, with maturity dates approximating the terms of the Group's obligations, and that are denominated in the currency in which the benefits are expected to be paid.

Remeasurements arising from defined benefit plans comprise actuarial gains and losses and the return on plan assets (excluding interest). The Group recognises them immediately in other comprehensive income and all other expenses related to defined benefit plans in administrative and marketing expenses in profit or loss.

When the benefits of a plan are changed, or when a plan is curtailed, the portion of the changed benefit related to past service by employees, or the gain or loss on curtailment, is recognised immediately in profit or loss when the plan amendment or curtailment occurs.

The calculation of the defined benefit obligations is performed by a qualified actuary using the projected unit credit method. When the calculation results in a benefit to the Group, the recognised asset is limited to the present value of benefits available in the form of any future refunds from the plan or reductions in future contributions and takes into account the adverse effect of any minimum funding requirements.

For defined contribution schemes, the amounts recognised in profit or loss are the contributions payable in the year.

m) Revenue recognition

Revenue is measured at the fair value of the consideration receivable less any discounts and excluding value added tax and other sales related taxes.

Roadside membership subscriptions and premiums receivable on underwritten insurance products are apportioned on a time basis over the period where the Group is liable for risk cover. The unrecognised element of subscriptions and premiums receivable, relating to future periods, is held within liabilities as deferred income and provision for unearned premium.

Commission income from insurers external to the Group is recognised at the commencement of the period of risk.

Where customers choose to pay by instalments, the Group charges interest based on the principal outstanding and disclosed interest rate and recognises this income over the course of the loan.

For all other revenue, income is recognised at point of delivery of goods or on provision of service. This includes work which has not yet been fully invoiced, provided that it is considered to be fully recoverable.

n) Insurance contracts

An insurance contract is a contract under which insurance risk is transferred to the issuer of the contract by another party. In the Roadside segment, the Group accepts insurance risk from its customers under roadside recovery service contracts by agreeing to provide services whose frequency and cost is uncertain. Claims and expenses arising from these contracts are recognised in profit or loss as incurred. The Group also has insurance risk within the insurance segment on insurance products underwritten by the Group.

At the balance sheet date, a liability adequacy test is performed to ensure the adequacy of the insurance contract liabilities. In performing these tests, current estimates of future cash outflows arising under insurance contracts are considered and compared with the carrying amount of deferred income, provision for unearned premiums and other insurance contract liabilities. Any deficiency is immediately recognised in profit or loss and an onerous contract provision is established.

The estimation of the ultimate liability from claims made under insurance contracts for breakdown recovery is not considered to be one of the Group's most critical accounting estimates. This is because there is a very short period of time between the receipt of a claim, e.g. a breakdown, and the settling of that claim. Consequently, there are no significant provisions for unsettled claims costs in respect of the roadside assistance services.

The provision for outstanding claims relating to products with insurance risk within insurance underwriting is set on an individual claim basis and is based on the ultimate cost of all claims notified but not settled, less amounts already paid by the reporting date, together with a provision for related claims handling costs. The provision also includes the estimated cost of claims incurred but not reported at the statement of financial position date ("IBNR"), which is set using statistical methods. Both outstanding claims and IBNR are not discounted for the time value of money. The amount of any anticipated reinsurance, salvage or subrogation recoveries is separately identified and reported within trade and other receivables and insurance contract liabilities respectively. Differences between the provisions at the reporting date and settlements and provisions in the following year are recognised in the income statement as they arise.

Reinsurance

The Group undertakes a programme of reinsurance in respect of the policies in which it underwrites. Outward reinsurance premiums are accounted for in the same accounting period as the related inward insurance premiums and are included as a deduction from earned premium, and therefore as a reduction in revenue. The amount of any anticipated reinsurance recoveries is treated as a reduction in claims costs.

o) Exceptional items and adjusted earnings per share

Exceptional operating items are events or transactions that fall within the operating activities of the Group and which by virtue of their size or incidence have been disclosed in order to improve a reader's understanding of the financial statements.

In addition, occasionally there are events or transactions that fall below operating profit that are one-off in nature and items within operating profit that relate to transactions that do not form part of the ongoing segment performance and which by virtue of their size or incidence have been separately disclosed in the financial statements.

Adjusted earnings per share adjusts profit after tax for items that are either discontinued operations, one-off in nature or relate to transactions that do not form part of the ongoing performance of the Group.

1 Basis of preparation and accounting policies (continued)

1.3 Accounting policies (continued)

p) Finance income and costs

Finance costs comprise interest payable, finance charges on finance leases recognised in profit or loss using the effective interest method, amortisation of debt issue fees, unwinding of the discount on provisions (including the net defined benefit obligations) and net foreign exchange losses that are recognised in the income statement (see foreign currency accounting policy).

Finance income comprises interest receivable on funds invested and net foreign exchange gains.

Foreign currency gains and losses are reported on a net basis.

q) Taxation

Tax on the profit or loss for the year comprises current and deferred tax.

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: the initial recognition of goodwill; the initial recognition of assets or liabilities that affect neither accounting nor taxable profit other than in a business combination; and differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilised. The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

r) Segmental analysis

The Group reports its operations using the segments that are reported for management purposes. Segments are based on business operations because this is where Group risk and return is focused.

s) Share-based payments

The Group operates a number of equity settled, share-based payment compensation plans for employees. The fair value of the equity settled awards is measured at the grant date based on expectations of performance conditions being met. The fair value of the awards is recognised as an expense with a corresponding credit to reserves.

t) Discontinued operations and disposals

A discontinued operation is a component of the Group's business, the operations and cash flows of which can be clearly distinguished from the rest of the Group and which:

› Represents a separate major line of business or geographical area of operations;

› Is part of a single coordinated plan to dispose of a separate major line of business or geographical area of operations; or

› Is a subsidiary acquired exclusively with a view to re-sale.

Classification as a discontinued operation occurs on disposal or when the operation meets the criteria to be classified as held for sale, if earlier.

When an operation is classified as a discontinued operation, the comparative statement of comprehensive income is represented as if the operation had been discontinued from the start of the comparative year.

u) Critical accounting estimates and judgements

Estimates are evaluated continually and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The Group makes estimates and assumptions about the future. The resulting accounting estimates will, by definition, seldom equal the related actual results.

Management have exercised judgement in applying the Group's accounting policies and in making critical estimates. The underlying assumptions on which these judgements are based, are reviewed on an ongoing basis and include the selection of assumptions in relation to the retirement benefit obligation and assumptions for future growth of cash flows to support the value-in-use calculations for the goodwill impairment review.

The principal estimates and assumptions that have a risk of causing an adjustment to the carrying amounts of assets and liabilities within the next financial period are discussed below.

Retirement benefit obligation

The Group's retirement benefit obligation, which is actuarially assessed each period, is based on key assumptions including return on plan assets, discount rates, inflation, future salary and pension costs. These assumptions may be different to the actual outcome.

Derivative financial Instruments

The fair value of derivative financial instruments is determined by reference to market values for similar financial instruments. The Group is therefore required to identify changes in market conditions around expectations for interest rates. These assumptions may be different to the actual outcome.

Contingent consideration

The Group calculates contingent consideration based on the probability weighted payout approach.

Goodwill

The Group tests goodwill for impairment annually. The recoverable amounts of cash generating units have been determined based on value-in-use calculations which require the use of estimates. Management has prepared discounted cash flows based on the latest strategic plan.

Share-based payments

The Group has issued a number of share-based payment awards to employees during the year which are measured at fair value. This involves estimates about the expected volatility of the share price and the number of leavers over the vesting period.

Notes to the Consolidated Financial Statements

continued

2 Segmental information

Following the recent strategic announcement and reflecting the way that the Group will be managed going forwards, the Group has determined that it has two key segments – Roadside and Insurance. Roadside incorporates the previous Roadside Assistance and Driving Services segments and Insurance will combine Insurance Services and Insurance Underwriting. Head Office costs have been allocated to these two key segments as these costs directly support the operations of these segments.

The Group has two reportable operating segments as follows:

› **Roadside:** This segment is the largest part of the AA business. The AA provides a nationwide service, sending patrols out to members stranded at the side of the road, repairing their vehicles where possible and getting them back on their way quickly and safely. In addition this segment includes the Group's publishing and hotels business, the AA and BSM driving schools and DriveTech which provides driver training and educative programs.

› **Insurance:** This segment includes the insurance brokerage activities of the AA, primarily in arranging motor and home insurance for customers, its home emergency activities and its intermediary financial services business. This segment also includes the insurance underwriting and reinsurance activities of the AA.

	2018 £m	2017 £m
Revenue		
Roadside	814	809
Insurance	145	131
Trading Revenue	959	940
Exceptional revenue provision (see note 21)	1	(7)
Group Revenue	960	933
Trading EBITDA		
Roadside	320	337
Insurance	71	66
Trading EBITDA	391	403
Share-based payments (see note 34)	(7)	(12)
Pension service charge adjustment	(10)	(8)
Amortisation and depreciation	(70)	(67)
Operating profit before exceptional items	304	316
Exceptional operating items (see note 5)	3	(32)
Operating profit	307	284
Net finance costs (see notes 6 and 7)	(166)	(184)
Profit before tax from continuing operations	141	100

All segments operate principally in the UK. Turnover by destination is not materially different from turnover by origin.

Segment performance is primarily evaluated using the Group's key performance measures of Trading Revenue and Trading EBITDA as well as operating profit before exceptional costs.

Trading Revenue is revenue on a continuing basis adjusted for exceptional items. Trading EBITDA is profit after tax on a continuing basis as reported, adjusted for depreciation, amortisation, exceptional operating items, share-based payments, pension service charge adjustments, net finance costs and tax expense. This better reflects the Group's underlying performance.

The pension service charge adjustment relates to the difference between the cash contributions to the pension scheme for ongoing contributions and the calculated annual service costs.

Exceptional items, net finance costs and tax expense are not allocated to individual segments as they are managed on a group basis.

Segmental information is not presented for items in the statement of financial position as management does not view this information on a segmental basis.

2 Segmental information (continued)

The segmental analysis based on the previous segmental view is as follows:

	2018 £m	2017 £m
Revenue		
Roadside Assistance	747	742
Insurance Services	133	131
Driving Services	67	67
Insurance Underwriting	12	–
Trading Revenue	959	940
Exceptional revenue provision (see note 21)	1	(7)
Group Revenue	960	933
Trading EBITDA		
Roadside Assistance	345	365
Insurance Services	79	76
Driving Services	22	20
Insurance Underwriting	1	(1)
Head Office costs	(56)	(57)
Trading EBITDA	391	403

Reconciliation of new segmental analysis

	Roadside		Insurance	
	2018 £m	2017 £m	2018 £m	2017 £m
Revenue				
Former segment presentation				
Roadside Assistance	747	742	–	–
Insurance Services	–	–	133	131
Driving Services	67	67	–	–
Insurance Underwriting	–	–	12	–
Trading Revenue	814	809	145	131

Operating profit before exceptional items

	Roadside		Insurance	
	2018 £m	2017 £m	2018 £m	2017 £m
Former segment presentation				
Roadside Assistance	345	365	–	–
Insurance Services	–	–	79	76
Driving Services	22	20	–	–
Insurance Underwriting	–	–	1	(1)
Head Office costs	(47)	(48)	(9)	(9)
Trading EBITDA	320	337	71	66
Share-based payments	(6)	(10)	(1)	(2)
Pension service charge adjustment	(8)	(7)	(2)	(1)
Amortisation and depreciation	(63)	(60)	(7)	(7)
Operating profit before exceptional items	243	260	61	56

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continued

3 Discontinued operations

On 11 August 2016, the Group completed the sale of its Irish business. The entities sold were AA Ireland Limited and its subsidiary undertakings. The Ireland business segment has therefore been reported as a discontinued operation as it represented a separate geographical area and the whole of the Irish operation was disposed of in the prior year.

As part of the transaction, the AA Ireland pension scheme, which is closed to future accrual, was transferred to AA Corporation Limited, a UK subsidiary of AA plc, and will continue to be the responsibility of the Group.

a) Results of discontinued operations

	2017 £m
Revenue	23
Expenses	(15)
Trading EBITDA	8
Depreciation and amortisation	(1)
Operating profit	7
Profit on disposal of discontinued operations	77
Profit before tax	84
Tax	(4)
Profit for the year from discontinued operations	80

Tax includes a charge of £1m in relation to the trading results of the discontinued operation and a charge of £3m in relation to tax due on the licensing of the brand to the Irish business segment.

No additional tax arose on the profit on disposal of the Irish business segment mainly due to the application of the substantial shareholding exemption.

The profit from the sale of the Ireland business segment consisted of the following:

	2017 £m
Proceeds	133
Fees	(3)
Net assets	(53)
Profit on disposal of discontinued operations	77

Proceeds, net of fees were £130m and allowed £106m of the Senior Term Facility to be repaid on 31 August 2016. Under the terms of our borrowings, we held back £24m from the net proceeds in ring-fenced available cash to be used for potential future acquisitions. The £24m was used to make a partial repayment of the STF on 13 July 2017.

b) Net cash flows of discontinued operations

	2017 £m
Operating cash flow	10
Investing cash flow	(3)
Total cash flows	7

During the prior year, the following cash flows arose as a result of Group acquisitions and disposals:

	2017 £m
Cash proceeds from sale of Irish business segment	133
Fees	(3)
Net cash proceeds from sale of Irish business segment	130
Cash held in Irish business at point of disposal	(31)
Acquisitions and disposals, net of cash acquired or disposed of	99

3 Discontinued operations (continued)

c) Net assets of discontinued operations at point of disposal

	2017 £m
Goodwill	26
Other intangible assets	9
Property, plant and equipment	3
Trade and other receivables	25
Cash and cash equivalents	31
Trade and other payables	(39)
Provisions – restructuring	(1)
Cumulative foreign exchange adjustment in reserves	(1)
Total	53

4 Operating profit

Operating profit from continuing operations is stated after charging:

	2018 £m	2017 £m
Amortisation of owned intangible assets	31	33
Depreciation of owned tangible fixed assets	14	12
Depreciation of leased tangible fixed assets	25	22
Operating lease rentals payable – land and buildings	3	4

5 Exceptional operating items

	2018 £m	2017 £m
Pension past service credit	34	–
Impairment of investment in joint venture (see note 14)	(1)	(1)
Duplicate breakdown cover	1	(7)
Impairment of goodwill (see note 26)	(27)	–
Other exceptional operating items	(4)	(24)
Total exceptional operating items	3	(32)

The Group has recognised a one-off pension past service credit of £34m as a result of the benefit changes implemented during the year (see note 25). This comprised a £12m gain from closure of the Final Salary sections of the AAUK scheme, due to the assumed deferred pension revaluation being lower than the assumed pensionable earnings increases, and a £22m gain from the change in pension indexation in the CARE section from RPI-based to CPI-based, which is expected to be lower in the long term.

Exceptional revenue included £1m for duplicate breakdown cover release (2017: £7m provision). In addition, £nil (2017: £3m) was charged to exceptional finance charges, bringing the total exceptional amount for duplicate breakdown cover to £1m release (2017: £10m provision). See note 21 for further information.

Other exceptional operating costs include £24m relating to business transformation costs (2017: £14m), £1m gain on disposal of fixed assets (2017: loss £3m), £2m for IT systems transformation (2017: £3m), £9m improvement in onerous properties position (2017: loss £1m), £6m gain on the disposal of the home services book (2017: £nil), £7m credit for the reversal of share based payment charge relating to the former Executive Chairman (see note 34) (2017: £nil), £1m relating to the loss on disposal of the VVCR entities (2017: £nil) and £nil mainly relating to non-recurring costs for cost restructuring activities (2017: £3m).

Costs from the current year refinancing in July 2017 and the prior period refinancing in December 2016 were directly attributable to the issue and repayment of loan notes and have therefore been included either in finance costs or in borrowings as debt issue fees (see notes 6 and 20).

Notes to the Consolidated Financial Statements

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6 Finance costs

	2018 £m	2017 £m
Interest on external borrowings	(132)	(147)
Finance charges payable under finance leases	(6)	(8)
Total ongoing cash finance costs	(138)	(155)
Ongoing amortisation of debt issue fees	(10)	(5)
Net finance expense on defined benefit pension schemes	(10)	(10)
Total ongoing non-cash finance costs	(20)	(15)
Debt repayment premium and penalties	(10)	(2)
Transfer from cash flow hedge reserve for extinguishment of cash flow hedge	2	(6)
Debt issue fees immediately written off following repayment of borrowings (see note 20)	(1)	(4)
Duplicate breakdown cover – interest on refunds (see note 21)	–	(3)
Exceptional finance costs	(9)	(15)
Total finance costs	(167)	(185)

Within interest on external borrowings is £7m (2017: £10m) of interest charged on the Senior Term Facility and £9m (2017: £8m) charged in relation to the interest rate swaps used to hedge the variable element of the Senior Term Facility (see note 20).

During the year, the Group repaid Class A1 notes of £175m (2017: £300m) and Class A4 notes of £55m (2017: £195m). As a result, the Group incurred an early repayment penalty of £10m (2017: £nil). As part of the refinancing during the prior year, the Group incurred a £2m premium cost in relation to the repayment of £165m of the Class B2 notes (see note 20). This premium was written off in the income statement.

During the year, there were £1m (2017: £4m) of amortised debt issue fees immediately written off following the refinancing.

During the year, the Group repaid £98m of the Senior Term Facility (2017: £106m) and made a non-cash adjustment to the cash flow hedge reserve of £2m. In the prior year, the Group transferred the fair value of the cash flow hedges related to the £106m repayment of the Senior Term Facility of £6m from other comprehensive income to the income statement.

7 Finance income

	2018 £m	2017 £m
Interest receivable	1	1
Total finance income	1	1

8 Staff costs

	2018 £m	2017 £m
Wages and salaries	245	251
Social security costs	26	25
Retirement benefit costs	33	29
Share-based payments expense	7	12
	311	317

The pension past service credit of £34m (2017: £nil) is excluded from retirement benefit costs above, see note 25.

The average monthly number of persons employed under contracts of service during the year was:

	2018	2017
Operational	6,028	6,266
Management and administration	1,193	1,188
	7,221	7,454

9 Tax

The major components of the income tax expense are:

	2018 £m	2017 £m
Consolidated income statement		
Current income tax		
Current income tax charge	23	21
Adjustments in respect of previous years	-	(1)
	23	20
Deferred tax		
Effect of tax rate change on opening balances	(1)	2
Origination and reversal of temporary differences	9	2
Adjustments in respect of prior years	(1)	2
	7	6
Tax expense in the income statement	30	26

	2018 £m	2017 £m
Consolidated statement of comprehensive income		
Tax on the effective portion of changes in fair value of cash flow hedges	3	1
Tax on remeasurements of defined benefit pension liability	21	(17)
Income tax charged/(credited) directly to other comprehensive income	24	(16)

Reconciliation of tax expense to profit before tax multiplied by UK's corporation tax rate:

	2018 £m	2017 £m
Profit before tax from continuing operations	141	100
Tax at rate of 19.1% (2017: 20.0%)	27	20
Adjustments relating to prior years	(1)	1
Rate change adjustment on temporary differences	(1)	2
Expenses not deductible for tax purposes:		
– Share-based payments	(1)	2
– Impairment of goodwill	5	-
– Other non-deductible expenses/non-taxed income	1	1
Income tax expense reported in the consolidated income statement at effective rate of 19.1% (2017: 22.0%)	30	26

In addition to the tax expense disclosed above, a charge of £nil (2017: £4m) has arisen on discontinued operations (see note 3).

The effective rate has been calculated by excluding the rate change adjustment that has arisen as a result of the future reduction in corporation tax rates affecting the carrying value of the deferred tax balances, the impact of share-based payments and the impairment of goodwill.

Deferred tax by type of temporary difference

	Consolidated statement of financial position		Consolidated income statement	
	2018 £m	2017 £m	2018 £m	2017 £m
Accelerated depreciation for tax purposes	8	8	-	1
Revaluations of land and buildings to fair value	(1)	(1)	-	-
Rollover relief	(2)	(2)	-	-
Pension	6	32	5	-
Revaluation of cash flow hedges	2	4	(1)	-
Short-term temporary differences	6	7	1	2
Losses available for offsetting against future taxable income	12	14	2	3
Deferred tax expense			7	6
Net deferred tax assets	31	62		

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9 Tax (continued)

Reconciliation of net deferred tax assets

	2018 £m	2017 £m
At 1 February	62	52
Tax expense recognised in the income statement	(7)	(6)
Tax (expense)/credit recognised in OCI	(24)	16
At 31 January	31	62

The Group offsets tax assets and liabilities if and only if it has a legally enforceable right to set off current tax assets and current tax liabilities and the deferred tax assets and deferred tax liabilities relate to income taxes levied by the same tax authority.

The UK corporation tax rate will reduce from 19% to 17% on 1 April 2020. These rates have been substantively enacted at the balance sheet date and have therefore been included in the deferred tax calculations.

Deferred tax has been recognised at an overall rate of 17.3% for the UK at 31 January 2018 (2017: 17.2%) and 12.5% for Ireland as at 31 January 2017. The UK rate has been adjusted to reflect the expected reversal profile of the Group's temporary differences.

The Group has brought forward tax losses which arose in the UK of £66m (2017: £76m) that are available indefinitely for offsetting against future taxable profits of the companies in which the losses arose. A deferred tax asset has been recognised in respect of these losses.

The new corporate interest restriction legislation was introduced with effect from 1 April 2017. As the majority of the Group activity is taxed within the UK these restrictions have not had a significant impact on the deductibility of the Group's interest. The residual interest disallowance has not resulted in a material increase in the tax charge above.

10 Earnings per share

Basic earnings per share amounts are calculated by dividing net profit for the year attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the year.

	2018	2017
Basic earnings per share:		
Profit after tax from total operations (£m)	111	154
Weighted average number of shares outstanding (millions)	610	609
Basic earnings per share from total operations (pence)	18.2	25.3

	2018	2017
Basic earnings per share:		
Profit after tax from continuing operations (£m)	111	74
Weighted average number of shares outstanding (millions)	610	609
Basic earnings per share from continuing operations (pence)	18.2	12.2

	2018	2017
Basic earnings per share:		
Profit after tax from discontinued operations (£m)	–	80
Weighted average number of shares outstanding (millions)	–	609
Basic earnings per share from discontinued operations (pence)	–	13.1

For diluted earnings per share, the weighted average number of ordinary shares is adjusted to assume conversion of all potential dilutive ordinary shares.

Under the Group's share incentive plan, shares are purchased monthly at market value and are therefore not dilutive. In addition, matching shares are issued monthly and placed into the employee benefit trust and are therefore not dilutive. As at 31 January 2018, there are no outstanding shares to be issued under these schemes that are potentially dilutive.

The Group has another class of potential dilutive ordinary shares relating to the MVP shares (see note 34). However, as at 31 January 2018, based on average market value of an ordinary share for the year, these are unlikely to vest and so were not dilutive.

There are no further classes of share that are dilutive as at 31 January 2018.

	2018	2017
Weighted average number of ordinary shares in issue (millions)	610	609
Potentially dilutive shares (millions)	–	–
Weighted average number of diluted ordinary shares (millions)	610	609
Diluted earnings per share from total operations (pence)	18.2	25.3
Diluted earnings per share from continuing operations (pence)	18.2	12.2
Diluted earnings per share from discontinued operations (pence)	–	13.1

10 Earnings per share (continued)

Adjusted earnings per share adjusts profit after tax for items that are either discontinued operations, one-off in nature or relate to transactions that do not form part of the ongoing performance of the Group.

	2018	2017
Profit after tax from continuing operations as reported (£m)	111	74
Adjusted for:		
Operating exceptional items (£m)	(3)	32
Share-based payment (£m)	7	12
Pension service charge adjustment (£m)	10	8
Exceptional finance costs (see note 6) (£m)	9	15
Tax expense (£m)	30	26
Adjusted profit before tax (£m)	164	167
Tax at the effective rate of 19.1% (2017: 22.0%) (£m)	(31)	(37)
Adjusted profit after tax (£m)	133	130
Weighted average number of shares outstanding (millions)	610	609
Adjusted basic earnings per share (pence)	21.8	21.3
Weighted average number of diluted ordinary shares (millions)	610	609
Adjusted diluted earnings per share (pence)	21.8	21.3

11 Goodwill and other intangible assets

	Goodwill £m	Software £m	Total £m
Cost			
At 1 February 2016	1,199	191	1,390
Additions	–	56	56
Disposals	–	(30)	(30)
Disposed with sale of subsidiary	(26)	(14)	(40)
At 31 January 2017	1,173	203	1,376
Additions	25	51	76
Disposals	(1)	–	(1)
At 31 January 2018	1,197	254	1,451
Amortisation and impairment			
At 1 February 2016	–	92	92
Amortisation	–	33	33
Amortisation within discontinued operations	–	1	1
Disposals	–	(29)	(29)
Disposed with sale of subsidiary	–	(5)	(5)
Exchange differences	–	1	1
At 31 January 2017	–	93	93
Amortisation	–	31	31
Impairment	27	–	27
At 31 January 2018	27	124	151
Net book value			
At 31 January 2018	1,170	130	1,300
At 31 January 2017	1,173	110	1,283

Within software, £32m (2017: £53m) relates to assets under construction which are not amortised.

Software additions comprise £12m (2017: £12m) in relation to internally developed assets and £39m (2017: £44m) in relation to separately acquired assets.

Goodwill additions of £25m (2017: £nil) relate to future growth prospects following the acquisition of Used Car Sites Limited (trading as AA Cars).

Goodwill disposals relate to the Group's Dutch VVCR driver training businesses, which were subsequently disposed of.

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12 Business combinations

Acquisitions during the year ended 31 January 2018

On 1 October 2017 the Group assumed control of Used Car Sites Limited (trading as AA Cars), a used car sales platform for a provisional consideration of £26m. At the point of acquisition Used Car Sites Limited had receivables of £1.8m, cash of £1.8m and payables of £2.4m. Used Car Sites Limited made a profit before tax of £nil for the year to 30 September 2017 and a profit before tax of £1m for the period 1 October 2017 to 31 January 2018.

On 1 March 2018 the Group completed the purchase of the entire share capital of Used Car Sites Limited. A payment of £12m was made to the former owners and £3m was paid into an escrow account and is payable to the former owners subject to certain conditions being met. These transactions cleared the balance of deferred consideration due within 1 year. This transaction left a remaining balance of £11m provisional deferred consideration which is due in more than one year based on the probability weighted payout approach. The range of potential contingent consideration is £nil-£21m. The assessment of goodwill arising on acquisition includes deferred consideration. The fair value attributed to the contingent deferred consideration is provisional as at 31 January 2018.

Acquisitions during the year ended 31 January 2017

There were no acquisitions during the year ended 31 January 2017.

13 Property, plant and equipment

	Freehold Land & Buildings £m	Long Leasehold Land & Buildings £m	Vehicles £m	Plant & equipment £m	Total £m
Cost					
At 1 February 2016	24	10	89	125	248
Additions	–	–	50	14	64
Disposals	–	–	(36)	(42)	(78)
Disposed with sale of subsidiary	–	(3)	(6)	(8)	(17)
Exchange differences	–	–	1	1	2
At 31 January 2017	24	7	98	90	219
Additions	–	–	40	14	54
Disposals	–	–	(34)	–	(34)
At 31 January 2018	24	7	104	104	239
Depreciation and impairment					
At 1 February 2016	7	4	22	93	126
Charge for the year	–	1	23	10	34
Disposals	–	–	(16)	(44)	(60)
Disposed with sale of subsidiary	–	(2)	(4)	(8)	(14)
Exchange differences	–	–	1	1	2
At 31 January 2017	7	3	26	52	88
Charge for the year	1	1	25	12	39
Disposals	–	–	(15)	–	(15)
At 31 January 2018	8	4	36	64	112
Net book value					
At 31 January 2018	16	3	68	40	127
At 31 January 2017	17	4	72	38	131

The net book amount of vehicles includes £68m (2017: £72m) held under finance lease agreements. The accumulated depreciation on these assets is £36m (2017: £26m).

The net book amount of other assets includes £nil (2017: £nil) in respect of plant and machinery held under finance lease agreements. The accumulated depreciation on these assets is £8m (2017: £8m).

Within plant and equipment £9m (2017: £4m) relates to assets under construction which are not depreciated.

14 Investments in joint ventures and associates

	2018			2017		
	Joint ventures £m	Associates £m	Total £m	Joint ventures £m	Associates £m	Total £m
At 1 February	6	4	10	6	4	10
Additions	-	-	-	1	1	2
Disposals	-	-	-	-	(1)	(1)
Share of profits	(1)	-	(1)	-	1	1
Dividend received	-	-	-	-	(1)	(1)
Impairment	(1)	-	(1)	(1)	-	(1)
At 31 January	4	4	8	6	4	10

The joint ventures of the Group which are indirectly held are detailed below.

Company	Country of registration	Nature of business
AA Law Limited (49% interest held) ¹	England	Insurance services
TVS Auto Assist (India) Limited (49% interest held) ²	India	Roadside services
Intelematics Europe Limited (32% interest held) ³	England	Roadside services

1 The Group exercises joint control over AA Law Limited through its equal representation on the Board.

2 The Group exercises joint control over TVS Auto Assist (India) Limited through its joint influence over key decision making.

3 The Group exercises joint control over Intelematics Europe Limited through its joint influence over key decision making.

The associates of the Group which are indirectly held are listed below.

Company	Country of registration	Nature of business
ARC Europe SA (20% interest held)	Belgium	Roadside services

During the prior year, the Group sold its interest in the shares of ACTA Assistance SA to ARC Europe SA. The other parties owning shares in ACTA Assistance SA and ARC Europe SA also sold their interest in ACTA Assistance for shares in ARC Europe so that the overall interest held in ARC Europe remained the same for each party. The Group also received a dividend from ACTA Assistance during the prior year of £1m.

During the year the Group's investment in TVS Auto Assist (India) Limited was impaired by £1m. On 30 March 2018, the Group sold its investment in this joint venture, see note 36.

15 Inventories

	2018 £m	2017 £m
Finished goods	7	6
	7	6

16 Trade and other receivables

	2018 £m	2017 £m
Current		
Trade receivables	137	141
Deferred consideration	3	-
Prepayments and accrued income	33	22
Reinsurers' share of insurance liabilities (see note 22)	24	28
Other receivables	4	4
	201	195
Non-current		
Deferred consideration	3	-

Included in trade receivables are amounts of £75m (2017: £70m) relating to amounts due from insurance broking customers.

Reinsurers' share of insurance liability comprises £5m (2017: £15m) unearned reinsurance premiums and £19m (2017: £13m) reinsurance claims outstanding.

Non-current receivables of £3m (2017: £nil) relate to deferred consideration following the disposal of the consumer home services business.

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17 Cash and cash equivalents

	2018 £m	2017 £m
Ring-fenced cash at bank and in hand – available	42	128
Ring-fenced cash at bank and in hand – restricted	8	8
Non ring-fenced cash at bank and in hand – available	79	60
Non ring-fenced cash at bank and in hand – restricted	21	15
	150	211

Ring-fenced cash and cash equivalents relate to cash held by AA Intermediate Co Limited and its subsidiaries. Dividends can only be paid to AA plc when certain debt to EBITDA and cash flow criteria are met.

Cash at bank and in hand includes £29m (2017: £23m) held by and on behalf of the Group's insurance businesses which are subject to contractual or regulatory restrictions.

18 Trade and other payables

	2018 £m	2017 £m
Current		
Trade payables	103	97
Other taxes and social security costs	18	27
Accruals	54	57
Deferred income	236	241
Deferred consideration	15	–
Provision for unearned premiums in Insurance Underwriting (see note 22)	14	18
Other payables	40	33
Obligations under finance lease agreements (see note 29)	48	47
	528	520
Non-current		
Deferred consideration	11	–

Included in trade payables are amounts of £66m (2017: £82m) relating to amounts due to underwriters in respect of insurance broking activities.

Current and non-current deferred consideration relates to the acquisition of Used Car Sites Limited, see notes 12 and 36.

19 Borrowings and loans

	2018 £m	2017 £m
Borrowings (see note 20)	2,727	2,799
Interest rate swap used for hedging (see note 27)	9	20
	2,736	2,819

The interest rate swap liability is shown on a net basis as the liability is settled with each counterparty on a net basis. On a gross basis, the asset is £8m (2017: £19m) and the liability is £17m (2017: £39m).

20 Borrowings

	Expected maturity date	Interest rate	Principal £m	Issue costs £m	Amortised issue costs £m	Total at 31 January 2018 £m	Total at 31 January 2017 £m
Senior Term Facility	31 July 2021	5.71%	250	(4)	3	249	347
Class A1 notes	31 July 2018	–	–	–	–	–	175
Class A2 notes	31 July 2025	6.27%	500	(1)	1	500	499
Class A3 notes	31 July 2020	4.25%	500	(3)	2	499	499
Class A4 notes	31 July 2019	–	–	–	–	–	55
Class A5 notes	31 January 2022	2.88%	700	(37)	8	671	664
Class A6 notes	31 July 2023	2.75%	250	(4)	–	246	–
Class B2 notes	31 July 2022	5.50%	570	(16)	8	562	560
		4.52%	2,770	(65)	22	2,727	2,799

20 Borrowings (continued)

At 31 January 2018, the Senior Term Facility carried interest at a rate of LIBOR plus a margin of 1.75%. The variable element has been fully hedged using matching interest rate swap arrangements which fix LIBOR at 3.96% until 31 July 2018, then 6.67% until 31 January 2019. All other borrowings have fixed interest rates. The weighted average interest rate for all borrowings of 4.52% has been calculated using the effective interest rate and carrying values on 31 January 2018. The net decrease of £72m in the carrying amount during the current year consists of £328m for repayment of loan notes and £250m issue of loan notes (see table below) and a £6m change in unamortised issue costs.

A summary of the Group's financing transactions is shown below:

	As at 1 February 2017	Issue/ repayment date 13 July 2017	As at 31 January 2018 £m
Senior Term Facility	348	(98)	250
Class A1 Notes	175	(175)	–
Class A2 notes	500	–	500
Class A3 notes	500	–	500
Class A4 notes	55	(55)	–
Class A5 notes	700	–	700
Class A6 notes	–	250	250
Class B2 notes	570	–	570
Total £m	2,848	(78)	2,770

In order to show the Group's net borrowing, the notes and the issue costs have been offset. Issue costs are shown net of any premium on the issue of borrowings. Interest rate swaps are recognised in the Consolidated Statement of Financial Position at fair value at the year end.

All of the Class A notes and Senior Term Facility are secured by first ranking security in respect of the undertakings and assets of AA Intermediate Co Limited and its subsidiaries. The Class A facility security over the AA Intermediate Co Limited group's assets ranks ahead of the Class B2 notes. The Class B2 notes have first ranking security over the assets of the immediate parent undertaking of the AA Intermediate Co Limited group, AA Mid Co Limited. AA Mid Co Limited group can only pay a dividend when certain net debt to EBITDA and cash flow criteria are met.

The Class B2 notes have an initial period to 31 July 2018 when any voluntary repayment would incur a make-whole payment and incur all remaining interest due to 31 July 2018. After this period, there is a further two year period when any voluntary repayment would be made at a fixed premium based on the date of redemption. Any voluntary early repayments of the Class A notes would incur a make-whole payment of all interest due to expected maturity date, except the Class A5 and Class A6 notes which can be settled without penalty within 3 months and 2 months respectively of the expected maturity date.

On 13 July 2017, the Group issued £250m of Class A6 notes at an interest rate of 2.75%. £4m of costs associated with the issue of the A6 notes were capitalised. This consisted of £1m of premium and £3m of new issue fees.

From the proceeds of the A6 notes, the Group repaid the remaining £175m of A1 notes incurring an interest penalty of £7m and £55m of A4 notes incurring an interest penalty of £3m. In line with the Group accounting policy, this was accounted for as an extinguishment of debt and therefore issue costs associated with the A1 and A4 notes have been written off but totalled under £1m.

Following the sale of the Irish business during the prior year (see note 3), we held back £24m from the net proceeds in ring-fenced available cash to be used for potential future acquisitions or repayment of debt. On 13 July 2017 the £24m was used as part of a repayment of £98m of the Senior Term Facility. This was treated as an extinguishment of debt and therefore the issue costs of just under £1m associated with the repayment were written off. The balance of the STF was renegotiated and its maturity extended to 31 July 2021. This was treated as a modification and therefore the fees associated with this, which were under £1m, were capitalised.

On the 13 July 2017 the working capital facility was reduced from £150m to £75m. The fees associated with this were under £1m and were written off.

In order to comply with the requirements of the Class A notes, we are required to maintain the Class A free cash flow to debt service ratio in excess of 1.35x and the senior leverage ratio below 5.5x. The Class B2 notes require us to maintain the Class B2 free cash flow to debt service ratio in excess of 1x.

The Class A and Class B2 notes therefore place restrictions on the Group's ability to upstream cash from the key trading companies to pay external dividends and finance activities unconstrained by the restrictions embedded in the debts.

The Class A notes only permit the release of cash providing the senior leverage ratio after payment is less than 5.5x and providing there is sufficient excess cash flow to cover the payment. The Class B2 notes only permit the release of cash providing the fixed charge cover ratio after payment is more than 2:1 and providing that the aggregate payments do not exceed 50% of the accumulated consolidated net income.

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21 Provisions and contingent liabilities

	Property Leases £m	Restructuring £m	Other £m	Duplicate breakdown cover £m	Total £m
At 1 February 2016	13	1	1	–	15
Utilised during the year	(1)	(1)	(1)	–	(3)
Transfer to discontinued operations	–	(1)	–	–	(1)
Charge for the year	5	4	–	10	19
At 31 January 2017	17	3	–	10	30
Utilised during the year	(2)	(2)	–	(8)	(12)
Released during the year	(9)	(1)	–	(1)	(11)
Charge for the year	–	10	–	–	10
At 31 January 2018	6	10	–	1	17
Current	2	10	–	1	13
Non-current	4	–	–	–	4
At 31 January 2018	6	10	–	1	17
Current	6	3	–	10	19
Non-current	11	–	–	–	11
At 31 January 2017	17	3	–	10	30

The property leases provision primarily relates to dilapidations. These sums are mainly expected to be paid out over the next 11 years, however, it will take 36 years to fully pay out all amounts provided for. The provision has been calculated on a pre-tax discounted basis. On 23 March 2018 the Group signed a settlement agreement to exit from the onerous Halfords service centres lease contracts, agreeing a final settlement of £2m.

The restructuring provision relates to redundancy and other related costs following the restructuring of operations in the current and prior periods.

Other provisions primarily comprised a provision for an onerous contract which was utilised in the previous financial year.

In the previous financial year, we became aware that there was some duplication of roadside assistance cover taken by a limited number of business-to-business customers who were personal members and held AVAs (Added Value Accounts) with our banking partners. We proposed a programme of remediation for them which has the support of the regulatory authority. While some were unaware that they had duplicate cover, others chose to maintain this to receive the benefits of membership. Through the review of data for the new Customer Relationship Management systems, we identified a group of customers for whom the benefit of holding both forms of cover was not clear. We proposed a programme of remediation for them which has the support of the regulatory authority. We provided a total of £10m for our estimate of the refunds due of which £7m was expected to relate to premiums previously paid for breakdown cover and £3m for interest payable on those premiums. During the period £5m has been paid out relating to premiums and £3m relating to interest, £1m has been released and we expect to pay out the remaining amount during the next financial year.

On 7 March 2018, the Group received notification that former Executive Chairman, Bob Mackenzie, who was dismissed for gross misconduct on 1 August 2017, had on 6 March 2018 issued a Claim Form in the High Court, Chancery Division against AA plc, its subsidiary Automobile Association Developments Limited and personally against a number of their directors and the Company Secretary. The Claim Form seeks a permanent injunction to retain his MVP shares and up to £225m in damages. As this litigation is active at the date of signing these financial statements, the Board have considered any potential financial impact. The Group has not made a provision for these amounts as the Group expects to be successful in rigorously defending these claims. However, the Group will incur legal costs of approximately £1m to defend these claims during the next two financial years which it would seek to recover from Bob Mackenzie when the litigation concludes.

22 Insurance Underwriting

Reconciliation to segmental result

	2018 £m	2017 £m
Gross earned premium	38	10
Reinsurance earned premium	(28)	(7)
Net earned premium	10	3
Deferral of broker commission	(1)	(3)
Other income	3	–
Insurance Underwriting revenue (see note 2)	12	–

22 Insurance Underwriting (continued)

	2018 £m	2017 £m
Gross claims incurred	(34)	(16)
Less reinsurance recoveries	22	14
Net claims paid	(12)	(2)
Administrative costs	3	(2)
Deferral of broker acquisition costs	(2)	3
Insurance Underwriting costs	(11)	(1)

Reconciliation of movements in the provision for unearned premiums

	2018 £m	2017 £m
Gross unearned premiums at 1 February	18	–
Less: unearned reinsurance premiums	(15)	–
Net unearned premiums at 1 February	3	–
Gross premiums written	34	28
Less: outward reinsurance premium	(18)	(22)
Net premiums written	16	6
Gross premiums earned	(38)	(10)
Less: reinsurance premium earned	28	7
Net premiums earned	(10)	(3)
Gross unearned premiums at 31 January (see note 18)	14	18
Less: unearned reinsurance premiums (see note 16)	(5)	(15)
Net unearned premiums at 31 January	9	3

Reconciliation of movements in claims outstanding

	2018 £m	2017 £m
Gross claims outstanding at 1 February	16	4
Less: reinsurance claims outstanding	(13)	(1)
Net claims outstanding at 1 February	3	3
Gross claims incurred	34	16
Less: reinsurance recoveries	(22)	(14)
Net claims incurred	12	2
Gross claims paid	(26)	(4)
Less: received from reinsurance	16	2
Net claims paid	(10)	(2)
Gross claims outstanding at 31 January (see below)	24	16
Less: reinsurance claims outstanding (see note 16)	(19)	(13)
Net claims outstanding at 31 January	5	3

Insurance technical provisions

	2018 £m	2017 £m
Outstanding claims provisions	18	10
Other technical provisions – provisions for incurred but not reported claims	6	6
	24	16

Provision is made for the estimated cost of claims incurred but not settled at the balance sheet date, including the cost of claims incurred but not yet reported. The estimated cost of claims includes expenses to be incurred in settling claims.

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23 Share capital

	2018 £m	2017 £m
Allotted, called up and fully paid		
610,807,568 (2017: 609,461,827) ordinary shares of £0.001 each	1	1
	1	1

The voting rights of the holders of all ordinary shares are the same and all ordinary shares rank pari passu on a winding up.

All movement in the number of shares relates to the issue of matching shares in relation to the staff share incentive plans (see note 34).

The MVP shares in issue were as follows:

	2018 £000	2017 £000
Allotted, called up and fully paid		
20,000,000 (2017: 20,000,000) MVP A shares of £0.001 each	20	20
20,000,000 (2017: 20,000,000) MVP B shares of £0.001 each	20	20
20,000,000 (2017: 20,000,000) MVP C shares of £0.001 each	20	20
	60	60

The MVP shares have no voting rights. There are 8 million authorised shares in each of the following MVP share classes: A1, B1 and C1. There are 12 million authorised shares in each of the following MVP share classes: A2, B2 and C2. In total, there are 60 million authorised MVP shares. See also note 34.

24 Reserves

	Share premium £m	Own shares £m	Currency translation reserve £m	Cash flow hedge reserve £m	Retained earnings £m	Total £m
At 1 February 2016	399	(22)	(1)	(10)	(2,323)	(1,957)
Retained profit for the year	–	–	–	–	154	154
Dividends paid	–	–	–	–	(55)	(55)
Purchase of own shares by the Employee Benefit Trust	–	(4)	–	–	–	(4)
Issue of shares	4	–	–	–	–	4
Share-based payments (see note 34)	–	–	–	–	12	12
Other comprehensive income:						
Exchange differences on translation of foreign operations	–	–	2	–	–	2
Remeasurement losses on defined benefit schemes (note 25)	–	–	–	–	(99)	(99)
Tax effect of remeasurement losses on defined benefit schemes (note 9)	–	–	–	–	17	17
Effective portion of changes in fair value of cash flow hedges	–	–	–	13	–	13
Tax effect of effective portion of changes in fair value of cash flow hedges (note 9)	–	–	–	(1)	–	(1)
At 31 January 2017	403	(26)	1	2	(2,294)	(1,914)
Retained profit for the year	–	–	–	–	111	111
Dividends paid	–	–	–	–	(56)	(56)
Purchase of own shares by the Employee Benefit Trust	–	(3)	–	–	–	(3)
Issue of shares	3	–	–	–	–	3
Other reserves	–	–	–	(2)	2	–
Other comprehensive income:						
Exchange differences on translation of foreign operations	–	–	(1)	–	–	(1)
Remeasurement gains on defined benefit schemes (note 25)	–	–	–	–	120	120
Tax effect of remeasurement gains on defined benefit schemes (note 9)	–	–	–	–	(21)	(21)
Effective portion of changes in fair value of cash flow hedges	–	–	–	8	–	8
Tax effect of effective portion of changes in fair value of cash flow hedges (note 9)	–	–	–	(3)	–	(3)
At 31 January 2018	406	(29)	–	5	(2,138)	(1,756)

24 Reserves (continued)

Currency translation reserve

The translation reserve comprises foreign exchange differences arising from the translation of the financial statements of foreign operations, as well as from the translation of liabilities that hedge the Group's net investment in a foreign subsidiary.

Cash flow hedge reserve

The cash flow hedge reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that have not yet occurred.

Dividends

In the year ended 31 January 2018, total dividends of 9.3p (2017: 9.1p) per qualifying ordinary share were paid. Dividends are paid from the unconsolidated distributable reserves of AA plc. As at 31 January 2018, the Company had distributable reserves of £531m (2017: £512m). In February 2018, the Directors proposed a final dividend of 1.4 pence per ordinary share (2017: 5.7p), representing total dividend payments of £30m for the 2018 financial year (2017: £57m). Subject to approval by shareholders at the AGM on 7 June 2018, the dividend will be paid on 12 June 2018 and will be accounted for as an appropriation of retained earnings in the 2019 financial year.

25 Pensions

The Group operates two funded defined benefit pension schemes: the AA UK Pension Scheme (AAUK) and the AA Ireland Pension Scheme (AAI). The assets of the schemes are held separately from those of the Group in independently administered funds. The AAUK scheme has closed final salary sections and a Career Average Revalued Earnings (CARE) section which provides for benefits to accrue on an average salary basis. Since 2004, new entrants to the AAUK scheme accrue benefits in the CARE section but the AAUK scheme was closed to new entrants from 1 October 2016. On 1 July 2017, accrual ceased under the final salary sections and members were moved to the CARE section for future accrual of benefits. In addition, pension indexation in the CARE section will now be based on CPI inflation, rather than RPI inflation, from April 2018 onwards. The AAI scheme is closed to new entrants and future accrual of benefits. During the prior year, following the sale of the Irish business by the Group (see note 3), AA Corporation Limited, a UK subsidiary of the Group, became the sponsor of the AAI scheme. The Group also operates an unfunded post-retirement Private Medical Plan (AAPMP), which is treated as a defined benefit scheme and is not open to new entrants.

The AAUK scheme is governed by a corporate trustee whose board is currently composed of member-nominated and company-nominated directors. The AAI scheme is governed by a corporate trustee whose board is currently composed of company-nominated directors of which some are also members of the scheme. For both pension schemes the company-nominated directors include an independent director whom the trustee board directors have nominated as Chairman. The Trustee of each scheme is responsible for paying members' benefits and for investing scheme assets, which are legally separate from the Group.

The AAUK and AAI schemes are subject to full actuarial valuations every three years using assumptions agreed between the Trustee of each scheme and the Group. The purpose of this valuation is to design a funding plan to ensure that the pension scheme has sufficient assets available to meet the future payment of benefits to scheme members.

The valuation of liabilities for funding purposes differs to the valuation for accounting purposes, mainly due to the different assumptions used and changes in market conditions between different valuation dates. For funding valuation purposes the assumptions used to value the liabilities are agreed between the Trustee and Group with the discount rate, for example, being based on a bond yield plus a margin based on the assumed rate of return on scheme assets. For accounting valuation purposes the assumptions used to value the liabilities are determined in accordance with IAS19 with the discount rate, for example, being based on high quality (AA rated) corporate bonds.

The valuations have been based on a full assessment of the liabilities of the schemes which have been updated where appropriate to 31 January 2018 by independent qualified actuaries.

The amounts recognised in the balance sheet are as follows:

	As at 31 January 2018			
	AAUK £m	AAI £m	AAPMP £m	Total £m
Present value of the defined benefit obligation in respect of pension plans	(2,491)	(50)	(45)	(2,586)
Fair value of plan assets	2,303	43	–	2,346
Deficit	(188)	(7)	(45)	(240)

	As at 31 January 2017			
	AAUK £m	AAI £m	AAPMP £m	Total £m
Present value of the defined benefit obligation in respect of pension plans	(2,515)	(53)	(59)	(2,627)
Fair value of plan assets	2,190	42	–	2,232
Deficit	(325)	(11)	(59)	(395)

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25 Pensions (continued)

The decrease in the deficit is due to the strong performance of plan assets, falling long-term inflationary expectations, changes in the demographic assumptions (reflecting the latest outlook for mortality rates), the past service credit in respect of the closure of the final salary sections and change to CPI-linked pension indexation for the CARE section within the AAUK scheme and Group contributions paid into the schemes. This was partially offset by falling discount rates over the period.

In June 2017, the Group completed the AAUK scheme triennial valuation as at 31 March 2016 agreeing a funding deficit of £366m with the pension trustees. The Group has committed to paying an additional £8m per annum from July 2017 to March 2019, £11m per annum from April 2019 to March 2021, uplifted in line with RPI from 1 April 2020 and £13m per annum from April 2021 to June 2026 uplifted in line with RPI from 1 April 2022 annually. In November 2013, the Group implemented an asset backed funding scheme which remains in place. The asset backed funding scheme provides a long-term deficit reduction plan where the Group makes an annual deficit reduction contribution of £13m increasing annually with inflation, until October 2038, secured on the Group's brands. The next triennial valuation of the AAUK scheme will take place as at 31 March 2019.

Using an inflation assumption of 3.1% and a discount rate assumption of 2.5%, the present value of the future deficit reduction contributions has been calculated. Based on these assumptions, the Group expects the present value of deficit reduction contributions to exceed the IAS 19 deficit. The Group notes that, in the event that a surplus emerges, it would have an unconditional right to a refund of the surplus assuming the gradual settlement of AAUK scheme liabilities over time until all members have left the scheme.

The Group has recognised a one-off past service credit of £34m as a result of the benefit changes described above. This comprised a £12m gain from closure of the Final Salary sections of the AAUK scheme, due to the assumed deferred pension revaluation being lower than the assumed pensionable earnings increases, and a £22m gain from the change in pension indexation in the CARE section from RPI-based to CPI-based, which is expected to be lower in the long term.

The last triennial valuation for the AAI scheme was as at 31 December 2016, the result of which was an increase in the going concern deficit with the contribution level remaining the same. The Group made deficit reduction contributions of c. £2m in the year ended 31 January 2018 and will continue to make annual deficit reduction contributions, increasing with inflation, until December 2023 or until an alternative agreement is signed with the trustees. The next triennial valuation of the AAI scheme will take place as at 31 December 2019.

In total, the Group is currently committed to pay c£22m in ongoing employer contributions and c£24m in deficit reduction employer contributions to its defined benefit plans (AAUK and AAI) in the year ending 31 January 2019.

In November 2017, the Group completed a full accounting valuation of the AAPMP with a valuation date of 31 January 2017. This updated the previous full accounting valuation of the AAPMP that was performed as at 31 January 2013 and was projected forward to relevant reporting dates.

The 31 January 2017 full accounting valuation of the AAPMP revealed a reduction in reported deficit as a result of the actual level of medical premium inflation experienced being lower than that assumed over the period between full valuations and the impact of the latest longevity expectations.

	Assets £m	Liabilities £m	Income statement £m	Statement of comprehensive income £m
Balance at 1 February 2017	2,232	(2,627)	-	-
Current service cost	-	(31)	(31)	-
Past service gain	-	34	34	-
Interest on defined benefit scheme assets/(liabilities)	61	(71)	(10)	-
Amounts recognised in the income statement	61	(68)	(7)	-
Effect of changes in financial assumptions	-	(56)	-	(56)
Effect of changes in demographic expectations	-	65	-	65
Effect of experience adjustment	-	38	-	38
Return on plan assets excluding interest income	73	-	-	73
Amounts recognised in the statement of comprehensive income	73	47	-	120
Foreign exchange gain/(loss)	1	(1)	-	-
Contribution from scheme participants	1	(1)	-	-
Benefits paid from scheme assets	(64)	64	-	-
Ongoing employer contributions	21	-	-	-
Deficit reduction employer contributions	21	-	-	-
Movements through cash	(21)	63	-	-
Balance at 31 January 2018	2,346	(2,586)	-	-

25 Pensions (continued)

	Assets £m	Liabilities £m	Income statement £m	Statement of comprehensive income £m
Balance at 1 February 2016	1,850	(2,146)	-	-
Current service cost	-	(29)	(29)	-
Interest on defined benefit scheme assets/(liabilities)	68	(78)	(10)	-
Amounts recognised in the income statement	68	(107)	(39)	-
Effect of changes in financial assumptions	-	(613)	-	(613)
Effect of changes in demographic expectations	-	110	-	110
Effect of experience adjustment	-	81	-	81
Return on plan assets excluding interest income	323	-	-	323
Amounts recognised in the statement of comprehensive income	323	(422)	-	(99)
Foreign exchange gain/(loss)	5	(6)	-	(1)
Contribution from scheme participants	1	(1)	-	-
Benefits paid from scheme assets	(55)	55	-	-
Ongoing employer contributions	20	-	-	-
Deficit reduction employer contributions	20	-	-	-
Movements through cash	(14)	54	-	-
Balance at 31 January 2017	2,232	(2,627)	-	-

Fair value of plan assets

The overall expected rate of return is calculated by weighting the individual rates in accordance with the anticipated balance in the plan's investment portfolio.

The table below shows the AAUK scheme assets split between those that have a quoted market price and those that are unquoted. Of the AAI scheme 43.5% (2017: 33.1%) of assets do not have a quoted market price.

The fair value of the AAUK plan assets and the return on those assets were as follows:

	2018		2017	
	Assets with a quoted market price £m	Assets without a quoted market price £m	Assets with a quoted market price £m	Assets without a quoted market price £m
Equities	174	352	184	258
Bonds/swaps	813	211	876	183
Property	88	183	81	168
Hedge funds	23	440	-	401
Cash/net current assets	17	2	37	2
Total AAUK scheme assets	1,115	1,188	1,178	1,012
Actual return on AAUK plan assets	132		388	

Investment strategy

The AAUK trustee determines its investment strategy after taking advice from a professional investment adviser. The AAUK scheme's investment strategy has been set following an asset/liability review which considered a wide range of investment opportunities available to the Scheme and how they might perform in combination. Other factors were also taken into account such as the strength of the employer covenant, the long term nature of the liabilities and the funding plan agreed with the employer.

The trustee aims to achieve the scheme's investment objectives through investing in a diversified portfolio of growth assets which, over the long term, are expected to grow in value by more than low risk assets like cash and gilts. This is done within a broad liability driven investing framework that uses such cash, gilts and other hedging instruments like swaps in a capital efficient way. In combination this efficiently captures the trustee risk tolerances and return objectives relative to the scheme's liabilities. A number of investment managers are appointed to promote diversification by assets, organisation and investment style.

To diversify sources of return and risk, the AAUK scheme invests in many asset classes and strategies, including equities, bonds and property funds which primarily rely on the upward direction of the underlying markets for returns, and also hedge funds which also invest in asset classes like equities, bonds and currencies, but in such a way that relies more on the skill of the investment manager to add returns whilst hedging against downward market moves.

The trustee's investment advisers carry out detailed ongoing due diligence on funds in all asset classes from both operational and investment capability standpoints and any funds which are not expected to achieve their investment performance targets are replaced where possible.

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25 Pensions (continued)

Pension plan assumptions

The principal actuarial assumptions were as follows:

	AAUK		AAI		AAPMP %	
	2018 %	2017 %	2018 %	2017 %	2018 %	2017 %
Pensioner discount rate	2.5	2.7	1.6	1.6	2.5	2.7
Non-pensioner discount rate	2.6	2.9	2.3	2.4	2.5	2.7
Pensioner RPI	3.3	3.5	–	–	3.3	3.5
Non-pensioner RPI	3.3	3.5	–	–	3.3	3.5
Pensioner CPI	2.2	2.4	1.6	1.5	2.2	2.4
Non-pensioner CPI	2.2	2.4	1.6	1.5	2.2	2.4
Rate of increase of pensions in payment (final salary sections) – pensioner	3.1	3.2	–	–	–	–
Rate of increase of pensions in payment (final salary sections) – non pensioner	3.1	3.2	–	–	–	–
Rate of increase of pensions in payment (CARE section) – pensioner	1.7	2.2	–	–	–	–
Rate of increase of pensions in payment (CARE section) – non pensioner	1.7	2.2	–	–	–	–
Pensioner increase for deferred benefits	2.2	2.4	1.6	1.5	–	–
Medical premium inflation rate	–	–	–	–	7.3	7.5

Mortality assumptions are set using standard tables based on scheme specific experience where available and an allowance for future improvements. For 2018, the assumptions used were in line with the SAPS (S2) series mortality tables (2017 – SAPS (S2) series) with future improvements in line with the CMI_2016 model with a 1.25% long-term rate of improvement (2017 – CMI_2015 model with a 1.5% long-term rate of improvement). The AAI scheme mortality assumptions are set using standard tables with scheme specific adjustments.

The AA schemes' overall assumptions are that an active male retiring in normal health currently aged 60 will live on average for a further 27 years and an active female retiring in normal health currently aged 60 will live on average for a further 29 years.

Sensitivity analysis

Reasonably possible changes at the reporting date to one of the relevant actuarial assumptions, holding other assumptions constant, would have affected the defined benefit liability by the amounts shown below:

	For the year ending 31 January 2018		
	AAUK £m	AAI £m	AAPMP £m
Increase of 0.25% in discount rate	126	2	2
Increase of 0.25% in Inflation rate	(100)	(1)	–
Increase of 1% in medical claims inflation	–	–	(9)
Increase of one year of life expectancy	(93)	(1)	–

An equivalent decrease in the assumptions at 31 January 2018 would have had the equal but opposite effect on the amounts shown above, on the basis that all other variables remain constant.

The weighted average duration of AAUK scheme liabilities at 31 January 2018 is around 21 years.

Pension scheme risks

The AAUK and AAI schemes have exposure to a number of risks because of the investments they make in following their investment strategy. Investment objectives and risk limits are implemented through the investment management agreements in place with the schemes' investment managers and monitored by the Trustees by regular reviews of the investment portfolios. In addition, under guidance from their investment advisers the Trustees monitor estimates of key risks on an ongoing basis such as those shown below. A number of measures are taken to mitigate these risks where possible.

Credit risk – this is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. This risk mainly relates to the schemes' bonds and is mitigated by carrying out due diligence and investing only in bond funds which are well diversified in terms of credit instrument, region, credit rating and issuer of the underlying bond assets. To reduce risk further, the underlying bond assets within a fund are ring fenced, and the scheme diversifies across a number of bond funds.

Currency risk – the scheme is subject to currency risk because some of the scheme's investments are in overseas markets. The Trustee hedges some of this currency risk by investing in investment funds which hold currency derivatives to protect against adverse fluctuations in the relative value of its portfolio positions as a result of changes in currency exchange rates.

25 Pensions (continued)

Market price risk – this is the risk that the fair value or future cash flows of a financial asset such as equities will fluctuate because of changes in market prices (other than those arising from interest rate, inflation or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market. The scheme manages this exposure to overall price movements by constructing a diverse portfolio of investments across various markets and investment managers.

Financial derivatives risk – The scheme does not directly hold any financial derivatives but instead invests in investment funds which hold the derivatives required to hedge the scheme's interest rate, inflation and currency risks. The scheme also permits some of the investment managers to use derivative instruments if these are being used to contribute to a reduction of risks or facilitate efficient portfolio management of their funds. The main risks associated with financial derivatives include: losses may exceed the initial margin; counterparty risk where the other party defaults on the contract; and liquidity risk where it may be difficult to close out a contract prior to expiry. These risks are managed by monitoring of investment managers to ensure they use reasonable levels of market exposure relative to initial margin and positions are fully collateralised on a daily basis with secure cash or gilts collateral.

The AAUK scheme had hedged around 60% of interest rate risk and around 65% of inflation risk (of the liabilities) as at 31 January 2018 as part of a policy to reduce financial risks to the Scheme. The current longer-term objective is to aim to hedge around 75% of both the interest rate risk and inflation risk of the liabilities; this will help to further reduce funding level volatility. More interest rate hedging will be added in due course as, and when, prevailing pricing is regarded as reasonable value in the circumstances, or if any other reasons drive a policy change on risk appetite.

26 Impairment of intangible assets

Goodwill acquired through business combinations has been allocated to cash-generating units ("CGUs") on initial recognition and for subsequent impairment testing. CGUs represent the smallest group of assets that independently generate cash flow and whose cash flow is largely independent of the cash flows generated by other assets.

The carrying value of goodwill by CGU is as follows:

	2018 £m	2017 £m
Roadside Assistance	874	874
Insurance Services	240	240
Driving Schools	–	26
AA Cars (see note 12)	25	–
DriveTech	31	33
	1,170	1,173

The Group has performed impairment testing at 31 January 2018 and 31 January 2017. The impairment test compares the recoverable amount of the CGU to its carrying value.

The recoverable amount of each CGU has been determined based on a value in use calculation using cash flow projections from the Group's three year plan up to 31 January 2021 and a reasonable expectation of growth in the subsequent two years. For the purposes of the impairment test, terminal values have been calculated using the Gordon growth model and a nil growth assumption which is lower than the expected long term average growth rate of the UK economy. Cash flows have been discounted at a pre-tax rate reflecting the time value of money and the risk specific to these cash flows. This has been determined as a pre-tax rate of 9.6% (2017: 9.0%).

The value in use calculation used is most sensitive to the assumptions used for growth and for the discount rate. Accordingly, stress testing has been performed on these key assumptions as part of the impairment test to further inform the consideration of whether any impairment is evident.

As a result of this review the Driving Schools' goodwill has been impaired by £26m (2017: £nil) and the DriveTech goodwill has been impaired by £1m (2017: £nil). In addition, DriveTech goodwill has been reduced by £1m (2017: £nil) following the disposal of the Group's Dutch driver training business.

27 Financial assets and financial liabilities

The carrying amount of all financial assets and financial liabilities by class are as follows:

Financial assets	2018 £m	2017 £m
Loans and receivables		
Cash and cash equivalents	150	211
Trade receivables	137	141
Deferred consideration	6	–
Other receivables and accrued income	21	16
Total financial assets	314	368

Notes to the Consolidated Financial Statements

continued

27 Financial assets and financial liabilities (continued)

Financial liabilities

	2018 £m	2017 £m
Measured at fair value through other comprehensive income		
Interest rate and fuel swaps used for hedging	9	20
Loans and borrowings		
Trade payables	103	97
Other payables	54	56
Deferred consideration	26	–
Obligations under finance lease agreements	64	67
Borrowings	2,727	2,799
Total financial liabilities	2,983	3,039

Fair values

Financial instruments held at fair value are valued using quoted market prices or other valuation techniques.

Valuation techniques include net present value and discounted cash flow models, and comparison to similar instruments for which market observable prices exist. Assumptions and market observable inputs used in valuation techniques include interest rates.

The objective of using valuation techniques is to arrive at a fair value that reflects the price of the financial instrument at each year end at which the asset or liability would have been exchanged by market participants acting at arm's length.

Observable inputs are those that have been seen either from counterparties or from market pricing sources and are publicly available. The use of these depends upon the liquidity of the relevant market. When measuring the fair value of an asset or a liability, the Group uses observable inputs as much as possible. Fair values are categorised into different levels in a fair value hierarchy based on the inputs used in the valuation as follows:

Level 1 – Quoted market prices in an actively traded market for identical assets or liabilities. These are the most reliable.

Level 2 – Inputs other than quoted prices included in Level 1 that are observable for the assets or liabilities. These include valuation models used to calculate the present value of expected future cash flows and may be employed either when no active market exists or when there are quoted prices available for similar instruments in active markets. The models incorporate various inputs including interest rate curves and forward rate curves of the underlying instrument.

Level 3 – Inputs for assets or liabilities that are not based on observable market data.

If the inputs used to measure the fair values of an asset or a liability might be categorised in different levels of the fair value hierarchy, then the fair value measurement is categorised in its entirety in the same level as the lowest input that is significant to the entire measurements.

The fair values are periodically reviewed by the Group Treasury function. The following tables provide the quantitative fair value hierarchy of the Group's interest rate swaps and loan notes.

The carrying values of all other financial assets and liabilities (including the Senior Term Facility) are approximate to their fair values:

At 31 January 2018:

	Carrying value £m	Quoted prices in active markets (Level 1) £m	Fair value measurement using	
			Significant observable inputs (Level 2) £m	Significant unobservable inputs (Level 3) £m
Financial liabilities measured at fair value				
Interest rate and fuel swaps (note 19)	9	–	9	–
Deferred consideration (due in more than one year)	11	–	11	–
Liabilities for which fair values are disclosed				
Loan notes (note 20)	2,478	2,639	–	–

At 31 January 2017:

	Carrying value £m	Quoted prices in active markets (Level 1) £m	Fair value measurement using	
			Significant observable inputs (Level 2) £m	Significant unobservable inputs (Level 3) £m
Financial liabilities measured at fair value				
Interest rate and fuel swaps (note 19)	20	–	20	–
Liabilities for which fair values are disclosed				
Loan notes (note 20)	2,452	2,656	–	–

There have been no transfers between the levels and no non-recurring fair value measurements of assets and liabilities during the two years to 31 January 2018.

28 Financial risk management objectives and policies

The Group's principal financial liabilities comprise borrowings as well as trade and other payables. The main purpose of these financial liabilities is to finance the Group's operations. The Group's principal financial assets include deposits with financial institutions, money market funds and trade receivables.

The Group is exposed to market risk, credit risk and liquidity risk. The Group's senior management oversees the management of these risks, supported by the Group Treasury function. The Group Treasury function ensures that the Group's financial risks are governed by appropriate policies and procedures and that financial risks are identified, measured and managed in accordance with the Group's policies and risk objectives. All derivative activities are for risk management purposes and are carried out by the Group Treasury function. It is the Group's policy not to trade in derivatives for speculative purposes.

The Board of Directors reviews and agrees policies for managing each of these risks, which are summarised below.

Market risk

Market risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in prices set by the market. The key market risk that the Group is exposed to is interest rate risk. The Group has policies and limits approved by the Board for managing the interest rate risk exposure. The Group's policy is to fully hedge all of its exposure to variable interest rates. The Group has therefore taken out interest rate swaps to the value of its variable rate instruments.

The interest rate profile of the Group's interest-bearing financial instruments is as follows:

	2018 £m	2017 £m
Fixed rate instruments		
Financial liabilities	(2,532)	(2,518)
Effect of interest rate swaps	(250)	(348)
Net exposure to fixed rate instruments	(2,782)	(2,866)
Variable rate instruments		
Financial liabilities	(249)	(347)
Effect of interest rate swaps	250	348
Net exposure to variable rate instruments	1	1

Sensitivity of fixed-rate instruments

The Group does not account for any fixed-rate financial assets and financial liabilities at fair value through profit or loss and does not use derivative instruments in fair value hedges. Consequently, having regard to fixed rate instruments, a change in market interest rates at the reporting date would not affect profit or loss.

Sensitivity of variable rate instruments

An increase of 50 basis points in interest rates at 31 January 2018 would have increased equity by £1m (2017: £2m) and would have had no impact on profit or cash because the Senior Term facility is hedged (see note 20). A decrease to interest rates of the same magnitude will have an equal and opposite effect on equity and profit. This calculation assumes that the change occurred at the year end and had been applied to risk exposures existing at that date.

This analysis assumes that all other variables remain constant and considers the effect of financial instruments with variable interest rates and the fixed rate element of interest rate swaps. The analysis is performed on the same basis for all comparative periods.

Credit risk

Credit risk is the risk that a counterparty will not meet its obligations under a financial instrument or customer contract, leading to a financial loss. The Group is exposed to credit risk in relation to its financial assets, outstanding derivatives and trade and other receivables. The Group assesses its counterparty exposure in relation to the investment of surplus cash and undrawn credit facilities. The Group primarily uses published credit ratings to assess counterparty strength and therefore to define the credit limit for each counterparty, in accordance with approved treasury policies.

The credit risk for the Group is limited as payment from customers is generally required before services are provided.

Credit risk in relation to deposits and derivative counterparties is managed by the Group's treasury function in accordance with the Group's policy. Investments of surplus funds are made only with approved counterparties and within credit limits assigned to each counterparty. The limits are set to mitigate financial loss through any potential counterparty failure.

The Group's maximum exposure to credit risk for the components of the statement of financial position at each reporting date is the carrying amount except for derivative financial instruments. The Group's maximum exposure for financial derivative instruments is noted under liquidity risk.

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continued

28 Financial risk management objectives and policies (continued)

The ageing analysis of trade receivables is as follows:

	Total £m	Neither past due nor impaired £m	Past due but not impaired		
			< 30 days £m	30 - 60 days £m	60+ days £m
2018	137	131	4	–	2
2017	141	135	4	–	2

The movements in the provision for the collective impairment of receivables are as follows:

	2018 £m	2017 £m
At 1 February	2	2
Charge for the year	3	2
Utilised	(1)	(1)
Unused amounts reversed	(1)	(1)
At 31 January	3	2

Liquidity risk

Liquidity risk is the risk that the Group either does not have available sufficient financial resources to enable it to meet its obligations as they fall due, or can secure them only at excessive cost. The Group's approach to managing liquidity risk is to evaluate current and expected liquidity requirements to ensure that it maintains sufficient reserves of cash and headroom on its working capital facilities.

The table below analyses the maturity of the Group's financial liabilities on a contractual undiscounted cash flow basis and includes any associated debt service costs. The analysis of non-derivative financial liabilities is based on the remaining period at the reporting date to the contractual maturity date.

At 31 January 2018:

	On demand £m	Less than 1 year £m	1-2 years £m	2-5 years £m	Over 5 years £m	Total £m
Loans and borrowings	–	117	117	2,282	832	3,348
Obligation under finance leases	–	52	10	7	–	69
Other payables and accruals	–	54	–	–	–	54
Insurance liabilities	24	–	–	–	–	24
Contingent consideration	–	–	6	5	–	11
Trade payables	–	103	–	–	–	103
	24	326	133	2,294	832	3,609

Interest rate swaps used for hedging

Assets (inflow)	–	(7)	–	–	–	(7)
Liabilities	–	19	2	3	–	24
	–	12	2	3	–	17
	24	338	135	2,297	832	3,626

At 31 January 2017:

	On demand £m	Less than 1 year £m	1-2 years £m	2-5 years £m	Over 5 years £m	Total £m
Loans and borrowings	–	126	641	1,536	1,195	3,498
Obligation under finance leases	–	51	13	8	–	72
Other payables and accruals	–	56	–	–	–	56
Insurance liabilities	16	–	–	–	–	16
Trade payables	–	97	–	–	–	97
	16	330	654	1,544	1,195	3,739

Interest rate swaps used for hedging

Assets (inflow)	–	(14)	(8)	–	–	(22)
Liabilities	–	23	18	–	–	41
	–	9	10	–	–	19
	16	339	664	1,544	1,195	3,758

28 Financial risk management objectives and policies (continued)

Capital management

As noted in the financial review on pages 27 to 31, the Group considers its capital to be a combination of net debt and equity.

	2018 £m	2017 £m
Total net debt	2,684	2,704
Equity (valued at close on 31 January)	770	1,486
Total capital	3,454	4,190

The Group's objectives when managing capital are:

- › to safeguard the entity's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders;
- › to put service, innovation and data at the heart of the AA;
- › to deliver targeted and strategic investment in our people, our products, our systems and operations;
- › to reduce Group borrowings and associated interest costs; and
- › to provide an adequate return to shareholders.

The relative priorities of these objectives are discussed on page 29 of the financial review.

The Group monitors capital using net debt to Trading EBITDA ratios. The key ratios are Senior Secured Debt to Trading EBITDA, and Net Debt to Trading EBITDA as calculated below:

	2018 £m	2017 £m
Senior Term Facility	250	348
Class A notes	1,950	1,930
Less: AA Intermediate Co Limited group cash and cash equivalents	(50)	(136)
Net Senior Secured Debt ¹	2,150	2,142
Class B2 notes	570	570
Finance lease obligations	64	67
Net WBS Debt ²	2,784	2,779
Less: AA plc cash and cash equivalents ³	(100)	(75)
Total Net Debt	2,684	2,704
AA plc Trading EBITDA	391	403
AA Intermediate Trading EBITDA ⁴	393	414
Net debt ratio ⁵	6.9x	6.7x
WBS leverage ratio ⁶	7.1x	6.7x
Senior leverage ratio ⁷	5.47x	5.2x

1 Principal amounts of the Senior Term Facility and Class A notes less AA Intermediate Co Limited group cash and cash equivalents.

2 WBS debt represents the borrowings and cash balances within the WBS structure headed by AA Intermediate Co Limited. This includes the principal amounts of the Senior Term Facility, Class A notes, Class B2 notes and finance leases less AA Intermediate Co Limited group cash and cash equivalents.

3 Total cash and cash equivalents for the Group excluding the value reported as the AA Intermediate Co Limited group cash and cash equivalents.

4 AA Intermediate Co Limited group Trading EBITDA including discontinued operations as required by the debt documents.

5 Ratio of Total Net Debt to AA plc Trading EBITDA for the last 12 months.

6 Ratio of Net WBS Debt to AA Intermediate Trading EBITDA for the last 12 months.

7 Ratio of Net Senior Secured Debt to AA Intermediate Trading EBITDA for the last 12 months.

The Senior Term Facility, Class A notes and Class B2 notes have interest cover covenants attached to them. The Group was in compliance with all covenants throughout the period and as at 31 January 2018.

The Group includes regulated companies which are required to hold sufficient capital to meet acceptable solvency levels based on the relevant regulators' requirements (see note 17). There are no other externally imposed capital requirements.

Further details on our policies and processes for managing capital as well as the thresholds set for the covenants above and our objectives to reduce group borrowings are set out in the financial review on pages 27 to 31.

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29 Commitments and contingencies

Operating lease commitments

Future minimum rentals payable under non-cancellable operating leases as at 31 January are as follows:

	Land and buildings	
	2018 £m	2017 £m
Leases expiring:		
Within one year	–	1
Between one and five years	3	10
After five years	37	23
	40	34
Rentals receivable from operating sub-leases	–	(4)
Amounts included in onerous lease provisions	(1)	(4)
	39	26

Where a property is no longer used by the Group for operational purposes, tenants are sought to reduce the Group's exposure to lease payments. Where the future minimum lease payments are in excess of any expected rental income due, a provision is made.

Finance lease commitments

The Group has finance lease contracts for vehicles and various items of plant and machinery. Future minimum lease payments under finance lease contracts together with the present value of the net minimum lease payments are as follows:

	2018		2017	
	Present value of payments £m	Minimum payments £m	Present value of payments £m	Minimum payments £m
Within one year	48	52	47	51
Between one and five years	16	17	20	21
Total minimum lease payments	64	69	67	72
Less amounts representing finance charge	–	(5)	–	(5)
Present value of minimum lease payments	64	64	67	67

Capital commitments

Amounts contracted for but not provided in the financial statements amounted to £22m (2017: £14m).

30 Subsidiary undertakings

The subsidiary undertakings of AA plc, all of which are wholly owned except where stated, are listed in note 9 of the Company financial statements.

31 Auditor's remuneration

	2018 £m	2017 £m
Amounts receivable by the Company's auditor and its associates in respect of:		
Audit of financial statements of subsidiaries of the Company	1	1

The fee for the audit of these financial statements was £0.2m (2017: £0.2m).

In addition, corporate finance services were provided by the Company's auditor which mainly relate to reporting accountant work that would normally be undertaken by the auditor. The fee for this work was £0.1m (2017: £0.4m).

32 Related party transactions

The following table provides the total value of transactions that have been entered into with associates during each financial year:

Transactions with associates:

Associate	Nature of transaction	2018 £m	2017 £m
ACTA SA	Call handling fees paid	–	2
ARC Europe SA	Registration and call handling fees	4	1

Note that the Group's direct interest in ACTA SA was sold in the prior year to ARC Europe SA, see note 14.

33 Compensation of key management personnel of the Group

Key management personnel are defined as those persons having authority and responsibility for planning, directing and controlling the activities of the Group.

Key management personnel consists of the Chief Executive Officer, Chief Financial Officer, Non-Executive Directors and the Executive Committee as well as the former Executive Chairman until his dismissal.

The amounts recognised as an expense during the financial year in respect of key management personnel are as follows:

	2018 £m	2017 £m
Short-term employee benefits	5	6
Share-based payments – MVP and LTBP shares (see note 34)	(2)	8
Total compensation paid to key management personnel	3	14

34 Share-based payments

	2018 £m	2017 £m
Share-based payments – MVP shares	4	8
Share-based payments – LTBP	1	2
Share-based payments – Retention	–	–
Share-based payments – staff share incentive plan	2	2
	7	12
Share based payments – MVP shares – exceptional operating item	(7)	–
Total share based payments	–	12

Management value participation shares (MVP shares)

On 23 June 2014, the Company issued 24 million convertible, redeemable MVP shares to certain key members of senior management at £0.001 per share. These shares were divided into three classes and are convertible into ordinary shares following satisfaction of a Total Shareholder Return (TSR) performance condition of 12% (or above) per annum compound growth against the admission price of £2.50 which is tested on the third, fourth and fifth anniversaries of admission to the London Stock Exchange.

A further 36 million MVP shares were issued at £0.001 per share on 22 December 2015.

14.2% of the issued MVP shares are held in the Employee Benefit Trust (EBT) and on 22 April 2016, awards were granted by the EBT to further key members of senior management over ordinary shares which convert from the remaining 14.2% (amounting to 8,520,000) MVP shares.

The MVP share-based payments are equity settled. The following table illustrates the number and fair value of the MVP shares:

	Vesting Date	2018 No. of shares	2017 No. of shares	2018 Fair value per share £	2017 Fair value per share £
June 2014 awards:					
A1 shares	23 June 2017	8,000,000	8,000,000	0.25	0.25
B1 shares	23 June 2018	8,000,000	8,000,000	0.26	0.26
C1 shares	23 June 2019	8,000,000	8,000,000	0.26	0.26
December 2015 awards:					
A2 shares	23 June 2017	9,160,000	9,160,000	0.38	0.38
B2 shares	23 June 2018	9,160,000	9,160,000	0.40	0.40
C2 shares	23 June 2019	9,160,000	9,160,000	0.40	0.40
April 2016 awards:					
A2 shares	23 June 2017	2,840,000	2,840,000	0.35	0.35
B2 shares	23 June 2018	2,840,000	2,840,000	0.35	0.35
C2 shares	23 June 2019	2,840,000	2,840,000	0.35	0.35
Total		60,000,000	60,000,000		

Unvested A1 and A2 shares can also be converted on the fourth or fifth anniversary of admission and unvested B1 and B2 shares can also be converted on the fifth anniversary of admission.

All MVP shares were valued using a Binomial model and 25% volatility assumption to calculate the fair value using risk-free interest rates ranging from 0.38% - 1.82%. The expected volatility reflects the assumption that the historical volatility is indicative of future trends which may not necessarily be the actual outcome.

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34 Share-based payments (continued)

Management value participation shares (MVP shares) (continued)

On 1 August 2017, the former Executive Chairman, who held 55% of the MVP shares, was dismissed for gross misconduct. Under the rules of the scheme he was deemed to be a bad leaver and therefore the Company has the right to request transfer (and failing compliance, transfer itself) all those MVP shares for a total consideration of 1 penny. The Company issued the transfer notice on 9 March 2018 and transferred the shares on 16 April 2018 to its Employee Benefit Trust. As per IFRS 2, the share-based payment charge in relation to his shares, has been reversed resulting in a credit to exceptional operating items in the income statement of £7m and a corresponding debit to equity.

Long Term Bonus Plan (LTBP)

As at 31 January 2018, the Company's EBT had issued 4 million conditional awards over market purchased ordinary shares to certain key members of senior management at nil cost. These shares were divided into three tranches, A, B and C and vest following satisfaction of a Total Shareholder Return (TSR) performance condition of 12% per annum compound growth against the admission prices which is tested on the third, fourth and fifth anniversaries of admission to the London Stock Exchange and satisfaction of certain individual performance targets.

If the awards over A shares do not vest on the third or fourth anniversary of admission, then they are retested on the fourth and fifth anniversary. If the awards over B shares do not vest on the fourth anniversary of admission, then they are retested on the fifth anniversary.

The fair values of awards were calculated using a Monte Carlo simulation model. The expected volatility range of 20% - 32% reflects the assumption that the historical volatility is indicative of future trends which may not necessarily be the actual outcome.

The LTBP share-based payments are equity settled. The following table illustrates the number and weighted fair values of the LTBP shares:

	Vesting date	2018 No. of shares	2017 No. of shares	2018 Weighted fair value per share £	2017 Weighted fair value per share £
A shares	26 June 2017	873,423	1,004,896	2.49	2.56
B shares	26 June 2018	859,069	993,060	1.98	2.07
C shares	26 June 2019	842,036	987,340	1.54	1.62
Total		2,574,528	2,985,296		

The number of ordinary shares over which awards are held has reduced by 410,768 due to leavers during the financial year. The difference between the 4 million issued awards and the current number of outstanding awards is due to leavers.

Retention Award

On 19 December 2017, the Company issued 2 million conditional awards over market purchased ordinary shares held by its Employee Benefit Trust to certain key members of senior management who were already in the LTBP scheme, at nil cost.

These shares were divided into two tranches, 1 and 2, and vest following satisfaction of a Total Shareholder Return (TSR) performance condition of 12% per annum compound growth against the issue price which is tested on 6 November 2018 and/or 6 November 2019 and satisfaction of certain individual performance targets.

The Retention award will lapse or partially lapse if the original LTBP awards vest in full or in part.

The fair values of awards were calculated using a Monte Carlo simulation model. The expected volatility range of 32%-36% reflects the assumption that the historical volatility is indicative of future trends which may not necessarily be the actual outcome.

The following table illustrates the number and fair values of the Retention Award shares:

	Vesting date	2018 No. of shares	2017 No. of shares	2018 Fair value per share £	2017 Fair value per share £
Tranche 1	6 November 2018	914,230	–	0.87	–
Tranche 2	6 November 2019	914,230	–	0.57	–
Total		1,828,460	–		

34 Share-based payments (continued)

Staff share incentive plans

The Group has a number of all employee Share Incentive Plans (SIP). Under the SIP, employees are able to buy Partnership shares by making weekly or monthly payments into the SIP. In addition, for every Partnership share an employee purchases, the Company will match this on a 1:1 basis (Matching Shares). The SIP share-based payments are equity settled. The following table illustrates the fair value and vesting period of the SIPs:

Share type	Award date	Vesting date	No. of shares 2018 ¹	Weighted fair value per share £
2015 SIP:				
Partnership shares	29 August 2014	29 August 2015	2,132,766	0.23
Matching shares	29 August 2014	29 August 2018	2,132,766	2.58
2016 SIP:				
Matching shares	See below	See below	1,366,211	2.20
2017 SIP:				
Matching shares	See below	See below	1,727,537	1.64
Total			7,359,280	

¹ The number of shares shown above is the estimated number.

The SIPs are valued using a Black Scholes model.

The expected volatility reflects the assumption that the historical volatility is indicative of future trends which may not necessarily be the actual outcome. SIP shares are issued on the 11th of each month with the vesting period of 36 months from the date they were issued.

Performance Share Plan (PSP)

During the year awards were granted under the PSP scheme to the CEO and other members of senior management. Further details on this scheme can be found in the remuneration report on page 75. As at 31 January 2018, no performance criteria had been set for these shares and therefore, as there was no shared understanding of the terms of the scheme, no IFRS 2 charge has been made.

35 Accounting standards, amendments and interpretations

New accounting standards, amendments and interpretations adopted in the year

In the year ended 31 January 2018, the Group did not adopt any new standards or amendments issued by the IASB or interpretations issued by the IFRS Interpretations Committee (IFRS IC) that have had a material impact on the consolidated financial statements. Other new standards, amendments and interpretations adopted, that have not had a material impact on the amounts reported in these financial statements but may impact the accounting for future transactions and arrangements, were:

IAS 1: Disclosure Initiative

Annual Improvements to IFRS 2012-2014

IFRS 11: Accounting for Acquisitions of Interests in Joint Operations

New accounting standards, amendments and interpretations not yet adopted

A number of new standards, amendments and interpretations, which have not been applied in preparing these financial statements, have been issued and are effective for annual reports beginning after 1 February 2017:

	Effective date
IFRS 15: Revenue from Contracts with Customers	1 January 2018
IFRS 9: Financial Instruments	1 January 2018
IFRS 2: Classification and Measurement of Share Based Payment Transactions – Amendments to IFRS 2	1 January 2018
IFRS 16: Leases	1 January 2019
IFRS 17: Insurance Contracts	1 January 2021

Management has completed a detailed impact assessment ahead of the implementation of IFRS 9, IFRS 15 and IFRS 16.

IFRS 9

Management's analysis has focused on receivables, hedging and the change in accounting options for debt issue fees.

It has been concluded that there will not be a material change to receivables as a result of the new standard and there will be no change to the Group's hedging policy.

Management has concluded that as a result of the change in accounting requirements regarding debt issue fees there will be a one-off gain of c£10m which will be recognised in opening retained earnings in line with IFRS 9.

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35 Accounting standards, amendments and interpretations (continued)

IFRS 15

Management have performed a detailed analysis of each Group revenue stream, with particular focus on our bundling arrangements and variable consideration. We do not believe that the conversion to IFRS 15 will lead to a material impact on the timing or value of revenue in any given period.

Management do anticipate a requirement for a more detailed disclosure providing greater disaggregation of our different revenue streams into categories that depict how the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors.

IFRS 16

Management expects the adoption of IFRS 16 to have a significant impact on the Group due to the number of property leases. The Group expects to adopt IFRS 16 from 1 February 2019 and will apply the standard retrospectively, with the cumulative impact of initially applying the standard recognised at 1 February 2019.

The initial impact assessment is that the adoption of IFRS 16 will result in:

➤ an additional finance lease liability of c£30m

➤ a tangible fixed asset of £20m to £30m (after adjusting for forecast onerous lease provisions and rent free accruals at 1 February 2019)

➤ increase in Trading EBITDA of c1% in FY20, representing rental expense which will now reduce the lease liability rather than being charged to the income statement

➤ additional depreciation and interest expense of c£4m in FY20

This impact assessment is based on current estimates of discount rate and also current expectations of the property portfolio at 1 February 2019. IFRS 16 requires lease liabilities to be discounted using the incremental borrowing rate on the date of initial application. The final impact of adoption of IFRS 16 cannot be determined before 1 February 2019.

The Group is currently assessing whether the other standards above will have a material impact on the financial statements for the year ended 31 January 2019.

36 Events after the reporting period

Bob Mackenzie Litigation

On 7 March 2018, the Group received notification that former Executive Chairman, Bob Mackenzie, who was dismissed for gross misconduct on 1 August 2017, had on 6 March 2018 issued a Claim Form in the High Court, Chancery Division against AA plc, its subsidiary Automobile Association Developments Limited and personally against a number of their Directors and the Company Secretary. The Claim Form seeks a permanent injunction to retain his MVP shares and up to £225m in damages. As this litigation is active at the date of signing these financial statements, the Board have considered any potential financial impact. The Group has not made a provision for these amounts as the Group expects to be successful in rigorously defending these claims. However, the Group will incur legal costs of approximately £1m to defend these claims during the next two financial years which it would seek to recover from Bob Mackenzie when the litigation concludes.

Other post balance sheet events

On 1 March 2018 the Group completed the purchase of the entire share capital of Used Car Sites Limited (trading as AA Cars). A payment of £12m was made to the former owners and £3m was paid into an escrow account and is payable to the former owners subject to certain conditions being met.

On 14 March 2018, the Group completed the sale of the entire share capital of its Dutch subsidiaries, VVCR Europe B.V., VVCR Europe Beroepsopleidingen B.V. and VVCR Europe Holding B.V. for a disposal cost of €32,000.

On 30 March 2018 the Group completed the sale of its 49% joint venture stake in TVS Auto Assist (India) Limited (see note 14) for cash consideration of £2m.

Company statement of financial position

as at 31 January

	Notes	2018 £m	2017 £m
Non-current assets			
Investment in subsidiaries	2	818	818
Investments in joint ventures	3	2	4
		820	822
Current assets			
Trade and other receivables	4	19	17
Cash at bank and in hand	5	79	60
		98	77
Total assets		918	899
Current liabilities			
Trade and other payables	6	(9)	(8)
Non-current liabilities			
Other payables	7	-	(1)
Total liabilities		(9)	(9)
Net assets		909	890
Equity			
Called up share capital	8	1	1
Share premium		406	403
Own shares		(29)	(26)
Retained earnings		531	512
Total equity attributable to equity holders of the parent		909	890

The profit for the financial year of the Company is £75m (2017: £60m).

As at 31 January 2018, the Company had distributable reserves of £531m (2017: £512m).

Signed for and on behalf of the Board on 16 April 2018 by

Simon Breakwell
Chief Executive Officer

Martin Clarke
Chief Financial Officer

The accompanying notes are an integral part of this company statement of financial position.

Company statement of changes in equity

	Share capital £m	Share premium £m	Own shares £m	Retained earnings £m	Total £m
At 1 February 2016	1	399	(22)	495	873
Profit for the year	–	–	–	60	60
Dividends	–	–	–	(55)	(55)
Issue of share capital	–	4	–	–	4
Purchase of own shares	–	–	(4)	–	(4)
Share-based payments	–	–	–	12	12
At 31 January 2017	1	403	(26)	512	890
Profit for the year	–	–	–	75	75
Dividends	–	–	–	(56)	(56)
Issue of share capital	–	3	–	–	3
Purchase of own shares	–	–	(3)	–	(3)
At 31 January 2018	1	406	(29)	531	909

The accompanying notes are an integral part of this company statement of changes in equity.

Notes to the Company financial statements

1 Authorisation of financial statements and Company accounting policies

1.1 Authorisation of financial statements

AA plc (the "Company") is a public limited company incorporated and domiciled in England and Wales. The Company's ordinary shares are traded on the London Stock Exchange.

These financial statements were prepared in accordance with Financial Reporting Standard 101 Reduced Disclosure Framework (FRS 101). The financial statements are prepared under the historical cost convention and on a going concern basis.

No profit and loss account is presented by the Company as permitted by Section 408 of the Companies Act 2006.

The accounting policies which follow set out those policies which apply in preparing the financial statements for the year ended 31 January 2018. The financial statements are prepared in sterling and are rounded to the nearest million pounds (£m).

1.2 Basis of preparation

The Company has taken advantage of the following disclosure exemptions under FRS 101:

- › IAS 1 paragraph 10(d) (statement of cash flows)
- › IAS 1 paragraph 16 (statement of compliance with all IFRS)
- › IAS 1 paragraph 38A (requirement for minimum of two primary statements, including cash flow statements)
- › IAS 1 paragraph 111 (cash flow statement information)
- › IAS 1 paragraphs 134-136 (capital management disclosures)
- › Paragraphs 45(b) and 46 to 52 of IFRS 2, 'Share-based payment'
- › IAS 7: 'Statement of cash flows'
- › IAS 8 paragraphs 30 and 31
- › The requirements in IAS 24, 'Related party disclosures' to disclose related party transactions entered into between two or more members of a group

1.3 Accounting policies

a) Foreign currencies

Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction or at the contracted rate if the transaction is covered by a forward foreign currency contract. Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the balance sheet date or if appropriate at the forward contract rate. All differences are taken to the profit and loss account.

b) Investments in subsidiaries and joint ventures

Fixed asset investments are included in the balance sheet at cost, less any provisions for permanent impairment.

Investments in subsidiaries and joint ventures are stated at the lower of cost and net realisable value.

The carrying amounts of the Company's assets are reviewed for impairment when events or changes in circumstances indicate that the carrying amount of the fixed asset may not be recoverable. If any such indication exists, the asset's recoverable amount is estimated. An impairment loss is recognised whenever the carrying amount of an asset or its income-generating unit exceeds its recoverable amount. Impairment losses are recognised in the profit and loss account unless it arises on a previously revalued fixed asset.

The recoverable amount of fixed assets is the greater of their net realisable value and value in use. In assessing value in use, the expected future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the rate of return expected on an investment of equal risk. For an asset that does not generate largely independent income streams, the recoverable amount is determined for the income-generating unit to which the asset belongs.

Joint ventures are joint arrangements whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement.

c) Critical accounting estimates and judgements

Estimates are evaluated continually and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The Group makes estimates and assumptions about the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The principal estimates and assumptions that have a risk of causing an adjustment to the carrying amounts of assets and liabilities within the next financial period are discussed below.

Management has exercised judgement in applying the Group's accounting policies and in making critical estimates. The underlying assumptions on which these judgements are based, are reviewed on an ongoing basis and include the assumptions for future growth of cash flows to support the value-in-use calculations for the investment impairment review.

Investments

The Group tests the investment balances for impairment annually. The recoverable amounts of the investments have been determined based on value-in-use calculations which require the use of estimates. Management has prepared discounted cash flows based on the latest strategic plan.

2 Investments in subsidiaries

	2018 £m	2017 £m
At 1 February	818	806
Charge for the share incentive schemes	-	12
Additions	4	-
Disposals	(2)	-
Share buyback	(2)	-
At 31 January	818	818

In the year ended 31 January 2018 there was an increase in investment in subsidiaries of £nil (2017: £12m) relating to the fair value of share-based payments granted. Details are provided in note 34 of the Group financial statements.

No indicators of impairment in the value of subsidiaries have been identified.

3 Investments in joint ventures

	2018 £m	2017 £m
At 1 February	4	4
Impairment	(2)	-
At 31 January	2	4

On 29 June 2015, the Company invested £4m in a 49% share of a joint venture with TVS Automobile Solutions, one of the largest players in the Indian automotive market. The Company sold its investment in the joint venture with TVS Automobile Associations on 30 March 2018 for cash consideration of £2m. Therefore the Company has impaired its investment to the net realisable value of £2m as at 31 January 2018.

4 Trade and other receivables

	2018 £m	2017 £m
Trade receivables from subsidiary undertakings	19	17
	19	17

Amounts owed by subsidiary undertakings are unsecured, have no repayment terms and bear no interest.

5 Cash

	2018 £m	2017 £m
Cash	79	60
	79	60

Notes to the Company financial statements

continued

6 Trade and other payables

	2018 £m	2017 £m
Amounts owed to subsidiary undertakings	8	8
Accruals	1	–
	9	8

Amounts owed to subsidiary undertakings are unsecured, have no repayment terms and bear no interest.

7 Other payables

	2018 £m	2017 £m
Other payables	–	1

8 Share capital

	2018 £m	2017 £m
Allotted, called up and fully paid		
610,807,568 (2017: 609,461,827) ordinary shares of £0.001 each	1	1
	1	1

The voting rights of the holders of all ordinary shares are the same and all ordinary shares rank pari passu on a winding up. AA plc has no authorised ordinary share capital.

The movement in the number of shares in the current year is in relation to the matching shares for the staff share incentive plans (see Group financial statements – note 34 for further information on these shares).

The Company has 60 million MVP shares in issue (see Group financial statements – note 34 for further information on these shares).

9 Subsidiary undertakings

All subsidiaries are wholly owned and incorporated and registered where stated below.

All subsidiaries are consolidated in the Group financial statements.

The principal subsidiary undertakings of the Company at 31 January 2018 are:

Name	Country
AA Acquisition Co Limited ²	United Kingdom
AA Bond Co Limited ³	Jersey
AA Corporation Limited ²	United Kingdom
AA Financial Services Limited ²	United Kingdom
AA Intermediate Co Limited ²	United Kingdom
AA Media Limited ²	United Kingdom
AA Mid Co Limited ^{1,2}	United Kingdom
AA Reinsurance Company Limited ^{1,4}	Guernsey
AA Senior Co Limited ²	United Kingdom
AA The Driving School Agency Limited ²	United Kingdom
AA Underwriting Insurance Company Limited ⁵	Gibraltar
Automobile Association Developments Limited ²	United Kingdom
Automobile Association Insurance Services Limited ²	United Kingdom
DriveTech (UK) Limited ²	United Kingdom
Intelligent Data Systems (UK) Limited ²	United Kingdom
VVCR Europe B.V. ⁶	Netherlands

1 Directly owned by AA plc, all other subsidiaries are indirectly held.

2 Company registered office: Fanum House, Basing View, Basingstoke, Hampshire, RG214EA, England.

3 Company registered office: 22 Greenville Street, St Helier, Jersey, JE4 8PX.

4 Company registered office: Heritage Hall, Le Marchant Street, St Peter Port, GY14JH, Guernsey.

5 Company registered office: First Floor, Grand Ocean Plaza, Ocean Village, Gibraltar.

6 Company registered office: Markeloseweg 94, 7461PB, 175, 7460AD, Rijssen, Nijverdal, Netherlands.

The other subsidiary undertakings of the Company at 31 January 2018 are:

Name	Country
A.A. Pensions Trustees Limited ²	United Kingdom
AA Brand Management Limited ²	United Kingdom
AA Garage Services Limited ²	United Kingdom
AA Insurance Holdings Limited ^{1,2}	United Kingdom
AA Ireland Pension Trustees DAC ³	Ireland
AA Pension Funding GP Limited ⁴	United Kingdom
AA Pension Funding LP ⁴	United Kingdom
AA Road Services Limited ²	United Kingdom
AA Technical Solutions Limited ²	United Kingdom
AA Underwriting Limited ²	United Kingdom
Automobile Association Holdings Limited ²	United Kingdom
Automobile Association Insurance Services Holdings Limited ²	United Kingdom
Automobile Association Protection and Investment Planning Limited ²	United Kingdom
Automobile Association Services Limited ²	United Kingdom
Automobile Association Underwriting Services Limited ²	United Kingdom
Breakdown Assistance Services Limited ⁶	United Kingdom
Breakdown Hero Limited ⁶	United Kingdom
Drakefield Group Limited ²	United Kingdom
Drakefield Holdings Limited ²	United Kingdom
Drakefield Insurance Services Limited ²	United Kingdom
Longacre Claims Limited ²	United Kingdom
Nationwide 4 X 4 Ltd ²	United Kingdom
Peak Performance Management Limited ²	United Kingdom
Personal Insurance Mortgages and Savings Limited ²	United Kingdom
The Automobile Association Limited ⁵	Jersey
VVCR Europe Beroepsopleidingen B.V. ⁷	Netherlands
VVCR Europe Holding B.V. ^{1,7}	Netherlands

1 Directly owned by AA plc, all other subsidiaries are indirectly held.

2 Company registered office: Fanum House, Basing View, Basingstoke, Hampshire, RG214EA, England.

3 Company registered office: 61a South William Street, Dublin 2, Ireland.

4 Company registered office: 50 Lothian Road, Festival Square, Edinburgh, EH3 9WJ, Scotland.

5 Company registered office: 22 Greenville Street, St Helier, Jersey, JE4 8PX.

6 Company registered office: 90 Long Acre, London, WC2E 9RA, England.

7 Company registered office: Markeloseweg 94, 7461PB, 175, 7460AD, Rijssen, Nijverdal, Netherlands.

10 Auditor's remuneration

The fee for the audit of these financial statements was £0.2m (2017: £0.2m).

11 Staff costs

The Company had no employees or employee staff costs in the current or prior year. However, the Company has incurred costs in respect of the Non-Executive Directors of £1m (2017: £1m).

Shareholder information

AA plc

Company number: 5149111

Registered office

Fanum House
Basing View
Basingstoke
Hampshire
RG214EA

Telephone: 0344 209 0754

Financial Calendar

2018 final dividend



3 May: Ex-dividend date

4 May: Record date

21 May: Last day to elect for DRIP



7 June: Annual General Meeting at Freshfields Bruckhaus Deringer LLP, Northcliffe House, 26-28 Tudor Street, London, EC4Y 0BQ

12 June: Dividend payment date/dividend reinvestment plan (DRIP) purchase

15 June: DRIP documents posted

2019 interim dividend



4 Oct: Ex-dividend date

25 Oct: Record date

19 Oct: Last day to elect for DRIP



9 Nov: Dividend payment date/DRIP purchase

14 Nov: DRIP documents posted

Share price information

The Company's ordinary shares are listed on the London Stock Exchange. Share price information can be found on the website www.theaapl.com

ISIN Number: GB00BMSKPJ95

SEDOL Number: BMSKRPJ9

Legal Entity Identifier: 213800DTPE4050I17349

Advisors

Corporate Brokers

Centos Securities, 678 Tokenhouse Yard, London EC2R 7AS
Liberum Capital, Ropemaker Place, Level 12, 25 Ropemaker Street, London, EC2Y 9LY
Morgan Stanley & Co, 20 Bank Street, Canary Wharf, London E14 4AD

Solicitors

Freshfields Bruckhaus Deringer LLP, 65 Fleet Street, London EC4Y 1HS
Proskauer Rose (UK) LLP, 110 Bishopsgate, London EC2N 4AY

Auditors

Ernst & Young LLP, 1 More London Place, London SE1 2AF

Please note that, subject to approval at the Annual General Meeting, scheduled to take place on 7 June 2018, PricewaterhouseCoopers LLP, 1 Embankment Place, London WC2N 6RH, will become the auditors of the Company.

Registrar

Enquiries and notifications concerning dividends, share certificates, transfers and address changes should be sent to the registrar:

Equiniti Limited

Equiniti Limited, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA.

0333 207 6538 (from outside the UK: +44 121 415 0999). Lines are open 8.30am to 5.30pm, Monday to Friday (excluding bank holidays in England and Wales).

You can access and maintain your AA plc shareholding online through our share portal www.shareview.co.uk

Online: www.shareview.co.uk

Financial public relations

Finsbury, The Adelphi, 1-11 John Adam Street, London, WC2N 6HT

E-communications

Shareholders can choose to receive all Company communications electronically. This environmentally friendly way of receiving information has a number of advantages including speedier delivery of documents and the ability to access reports and results on the internet wherever you are. To register please visit the share portal at www.shareview.co.uk.

Dividend reinvestment plan (DRIP)

The Company offers a DRIP to shareholders as a cost-efficient way of increasing their shareholding in the Company. Should you wish to participate in the DRIP please contact the registrar to request a mandate form and an explanatory booklet. Your completed mandate form must be received by the registrar no later than 21 May 2018 if you wish your final dividend for the year to be reinvested to buy additional shares.

Shareholder information

continued

Keep your personal details up to date

Please remember to tell our registrar, Equiniti, if you move or need to update your bank or building society details.

If you hold 2,500 shares or fewer, you can update details quickly and easily over the telephone using the Equiniti contact details above. If you hold more than 2,500 shares you will need to write to Equiniti.

Managing your shares online

You can go online to manage your shareholding by registering for Shareview, the online portal, where you can:

1. receive the latest updates from the AA direct to your email
2. update your address and bank details online
3. vote in advance of general meetings

To register for Shareview, please follow these three easy steps:

1. Go to www.shareview.co.uk
2. Register for electronic communication by following the instructions on screen
3. You will then be sent an activation code in the post the next working day

Identity theft

Identity theft is on the increase. Criminals may steal your personal information, putting your AA plc shareholding at risk.

Tips for protecting your shares:

- › ensure all your certificates are kept in a safe place or hold your shares electronically in CREST via a nominee
- › keep all correspondence from the registrar that shows your shareholder investor code in a safe place, or destroy your correspondence by shredding it
- › if you change address, inform the registrar in writing or via our share portal at www.shareview.co.uk
- › know when dividends are paid and consider having your dividend paid directly into your bank account. This will reduce the risk of the cheque being intercepted or lost in the post. If you change your bank account, inform the registrar of the details of your new account. You can do this by post or online using our share portal at www.shareview.co.uk. Respond to any letters the registrar sends you about this
- › if you receive a letter from the registrar regarding a change of address or a dividend instruction but have not recently moved or requested a change to how you receive your dividends please contact the registrar using the opposite contact details immediately as you may have been a victim of identity theft
- › if you are buying or selling shares only deal with registered brokers

Share fraud warning

Remember: if it sounds too good to be true, it probably is.

You should be very wary of any unsolicited advice, offers to buy shares at a discount or offers of free company reports.

In recent years, many companies have become aware that their shareholders have received unsolicited telephone calls or correspondence concerning investment matters. These are typically from overseas based 'brokers' working in 'boiler rooms' who target UK shareholders, offering to sell them what often turn out to be worthless or high risk shares in US or UK investments. These brokers can be very persistent, extremely persuasive and use sophisticated means to approach and convince investors. The Financial Conduct Authority (FCA) has found that even experienced investors have been caught out by share fraud. It was also discovered that, on average, victims of boiler rooms lose an average of £20,000 to these scams, with as much as £200 million being lost in the UK each year.

If you receive any unsolicited investment advice, you should follow the steps below:

- › avoid getting into a conversation, note the name of the person and firm contacting you and then end the call
- › check that they are properly authorised by the FCA before getting involved via its register: www.fca.org.uk/register or call 0800 111 6768
- › search the list of unauthorised firms to avoid: www.fca.org.uk/scams
- › think about getting independent financial and professional advice before you hand over any money. Details of any share dealing facilities that the Company endorses will be included in Company mailings

Protecting your investment

We strongly advise you to deal only with financial services firms that are authorised by the FCA. Keep in mind that authorised firms are unlikely to contact you out of the blue with an offer to buy or sell shares. If you deal with an unauthorised firm, you would not be eligible to receive payment under the Financial Services Compensation Scheme.

For more information, visit the FCA website: www.fca.org.uk/scams

Reporting a scam

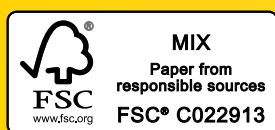
If you suspect you have been approached about an investment scam, contact the FCA using the share fraud reporting form: www.fca.org.uk/scams. You can also call the FCA Consumer Helpline on 0800 111 6768. Reporting unauthorised organisations who are targeting, or have targeted, UK investors, means the FCA can maintain an up to date list and appropriate action can be considered.

If you have already paid money to share fraudsters you should contact Action Fraud, the UK's national reporting centre for fraud and internet crime, on 0300 123 2040 or online at www.actionfraud.police.uk. The service is run by the City of London Police working alongside the National Fraud Intelligence Bureau.

Shareholder queries and information

Financial information about the Company including the annual report, regulatory announcements and corporate governance information is available on our website: www.theaapl.com

Alternatively, please contact us at investorrelations@theaa.com



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This report has been printed on Chorus Lux Silk which is FSC® certified and made from 100% Elemental Chlorine Free (ECF) pulp. The mill and the printer are both certified to ISO 14001 environmental management system and registered to EMAS the eco management Audit Scheme. The report was printed using vegetable based inks by a CarbonNeutral® printer.

